



HONG KONG MONETARY AUTHORITY

**Briefing to the Legislative Council
Panel on Financial Affairs**

6 May 2019



DISCUSSION TOPICS

Updates on

- Financial and Economic Environment
- Currency Stability
- Banking Stability
- Financial Infrastructure
- Hong Kong as an International Financial Centre
- Investment Environment and Performance of the Exchange Fund
- Hong Kong Mortgage Corporation



FINANCIAL AND ECONOMIC ENVIRONMENT



GLOBAL ECONOMIC GROWTH FORECASTS

Real GDP Growth

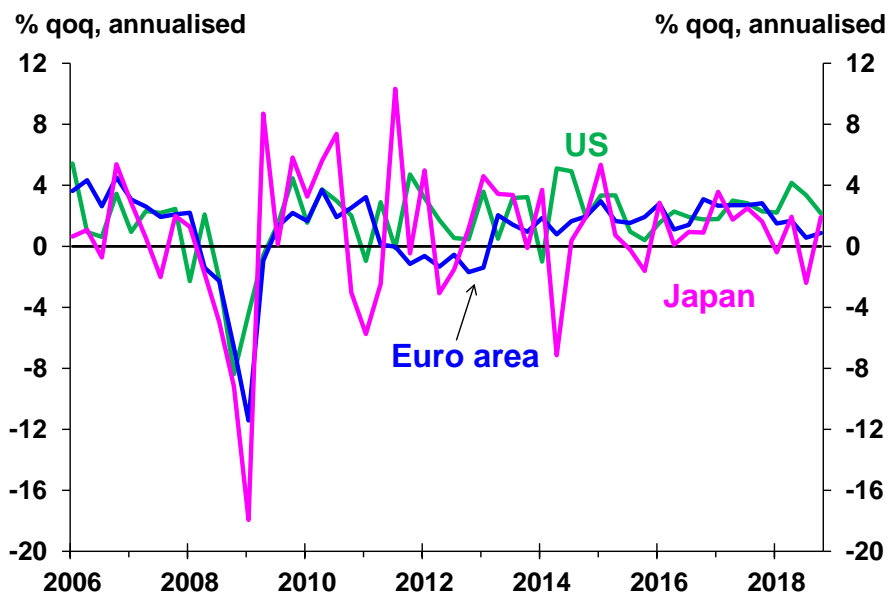
(% year-on-year)

	2018	2019 Forecasts	2020 Forecasts
US	2.9	2.4	2.0
Euro area	1.8	1.1	1.3
Japan	0.8	0.6	0.5
Asia (ex-Japan)	5.8	5.5	5.4
Mainland China	6.6	6.2	6.1
Hong Kong	3.0	2.2	2.3

Sources: April Consensus Forecasts and Official Statistics



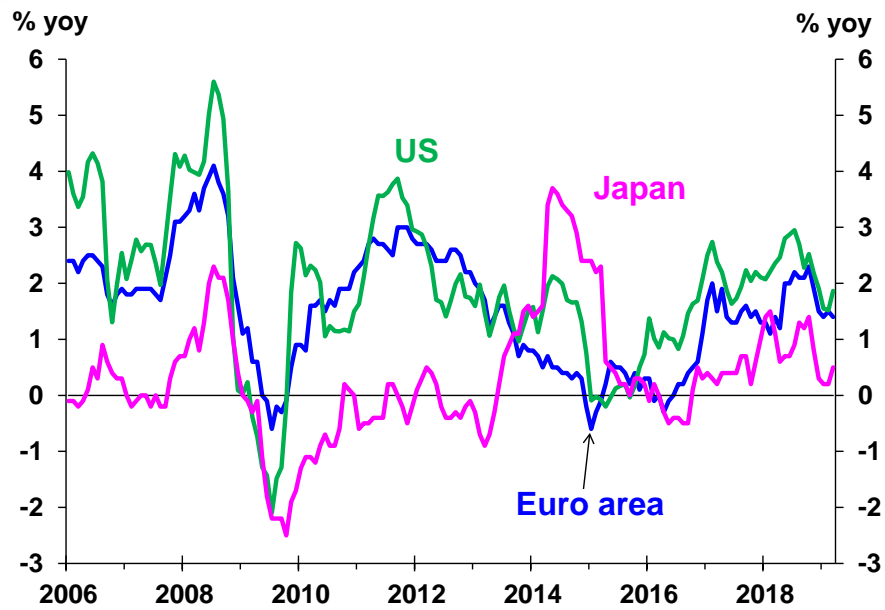
REAL GDP GROWTH IN MAJOR ECONOMIES



Source: CEIC



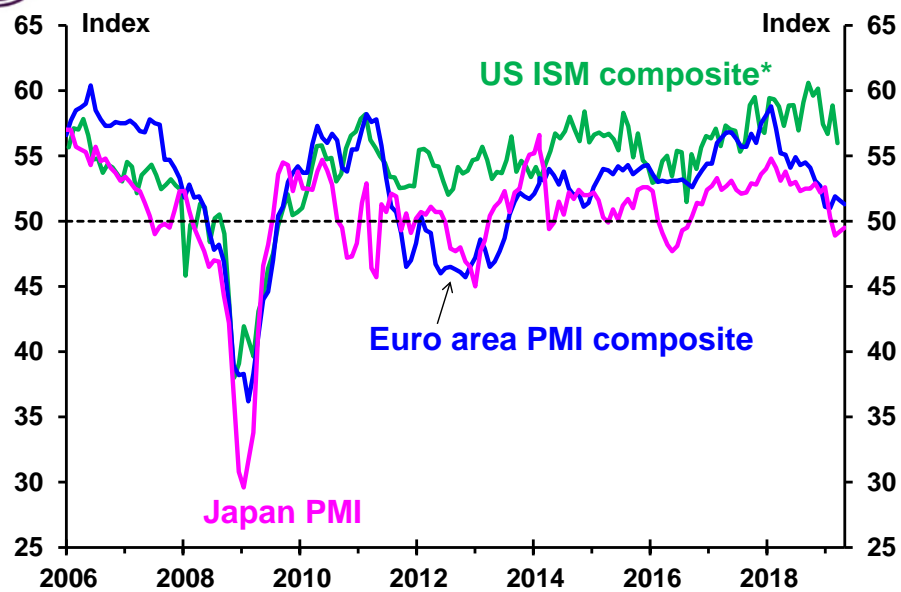
HEADLINE INFLATION IN MAJOR ECONOMIES



Source: CEIC



PURCHASING MANAGERS' INDEX IN MAJOR ECONOMIES

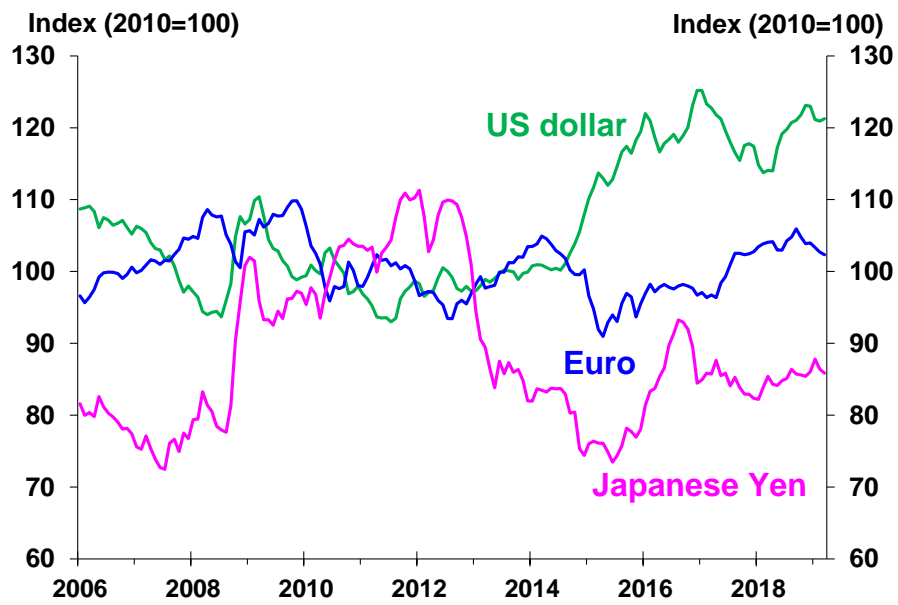


*Weighted average of the ISM manufacturing and non-manufacturing indices

Sources: Bloomberg and CEIC



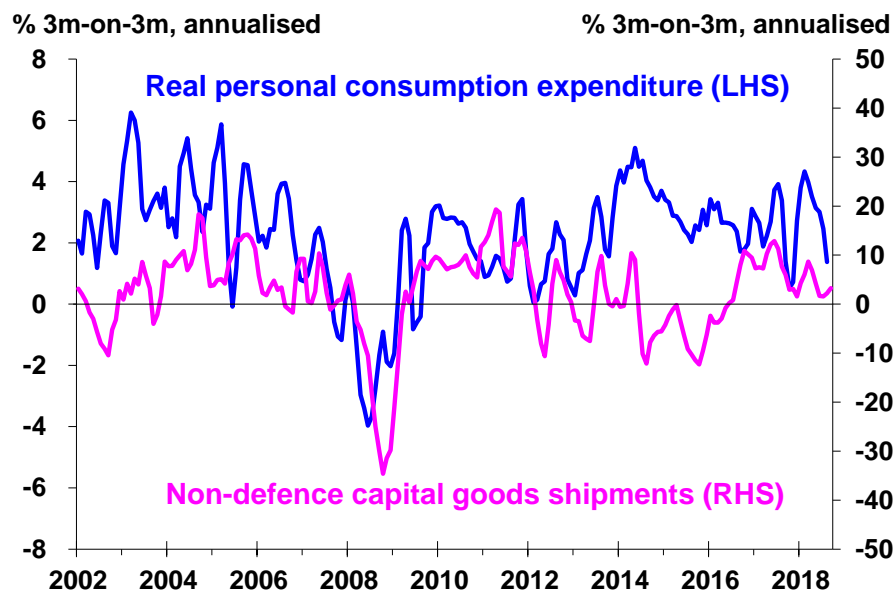
NOMINAL EFFECTIVE EXCHANGE RATE INDEX OF MAJOR CURRENCIES



Source: CEIC



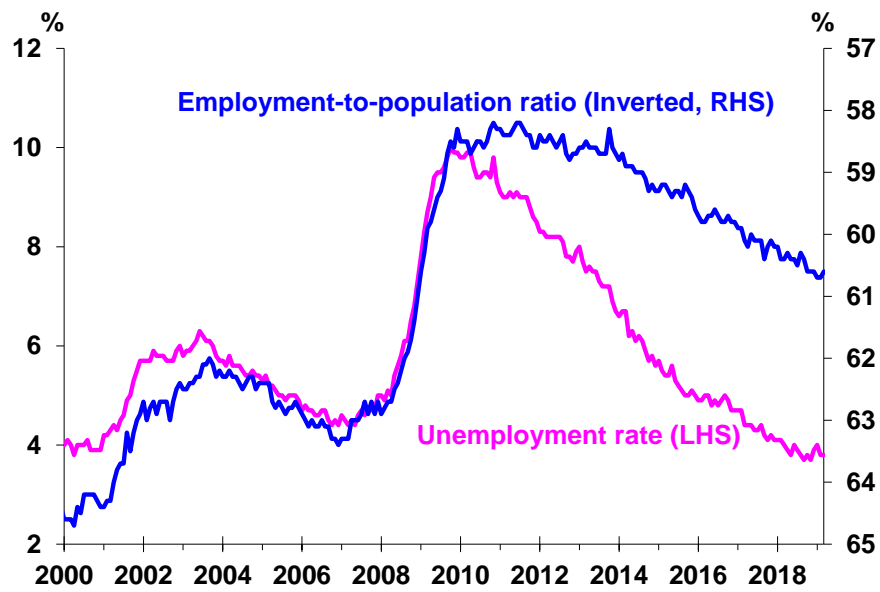
US: CONSUMPTION GROWTH & BUSINESS INVESTMENT ACTIVITY



Source: CEIC



US: LABOUR MARKET SITUATION



Source: CEIC



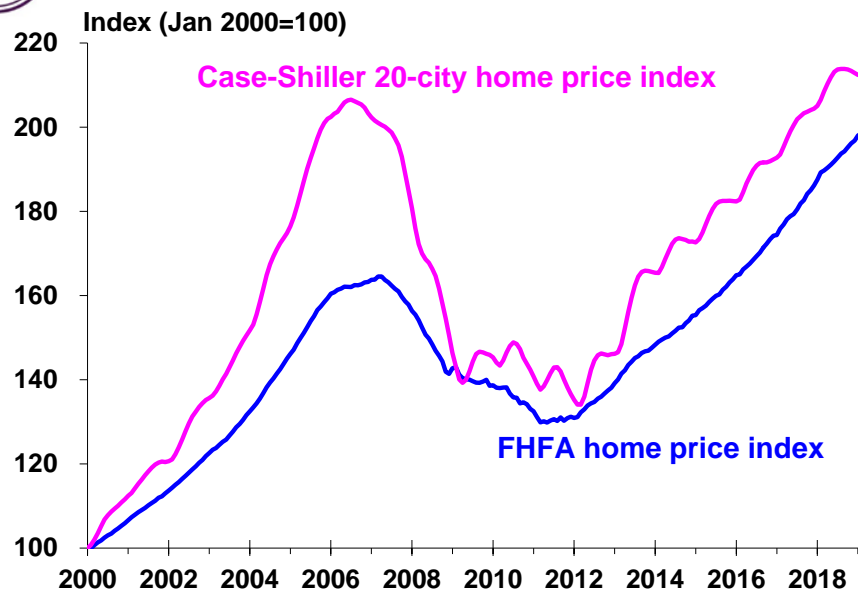
US: LABOUR FORCE PARTICIPATION



Source: CEIC



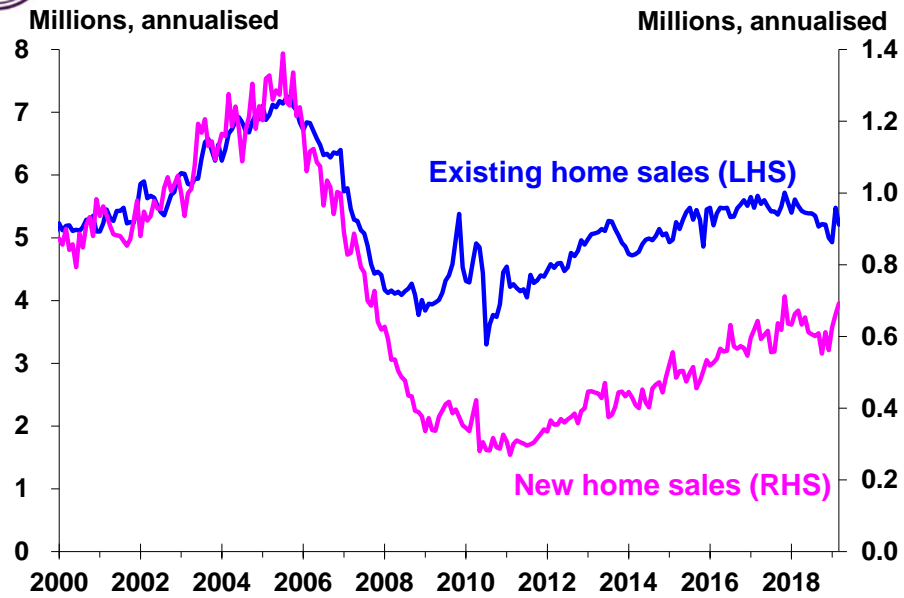
US: HOME PRICES



Sources: CEIC and Datastream



US: HOME SALES

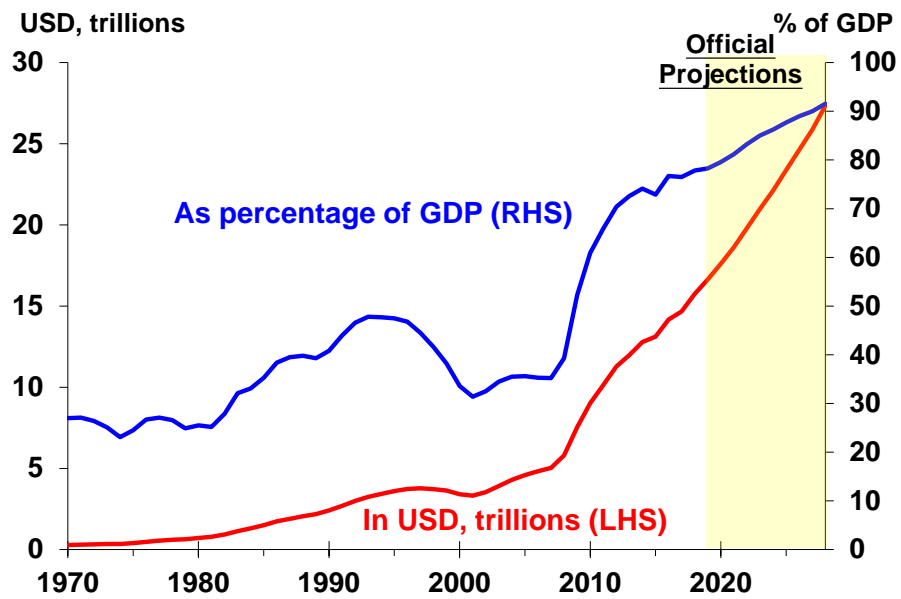


Source: CEIC



US: FEDERAL GOVERNMENT DEBT

US federal debt held by the public

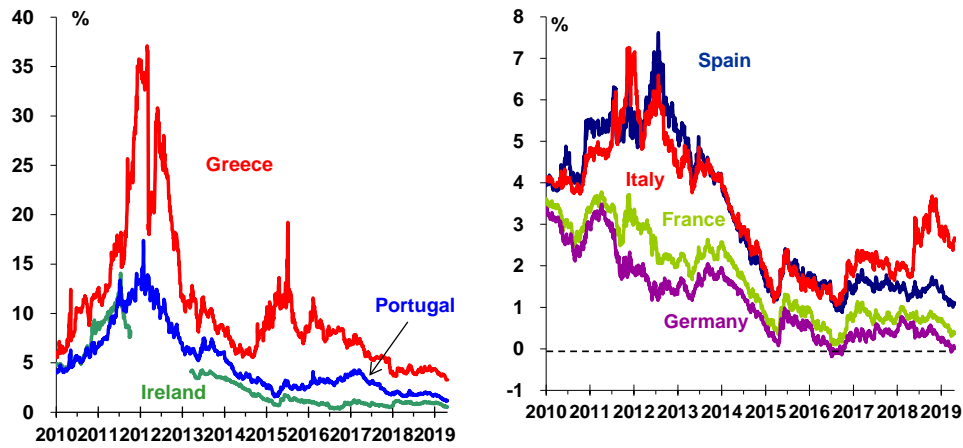


Sources: CEIC and Congressional Budget Office



EURO AREA: SOVEREIGN BOND YIELDS

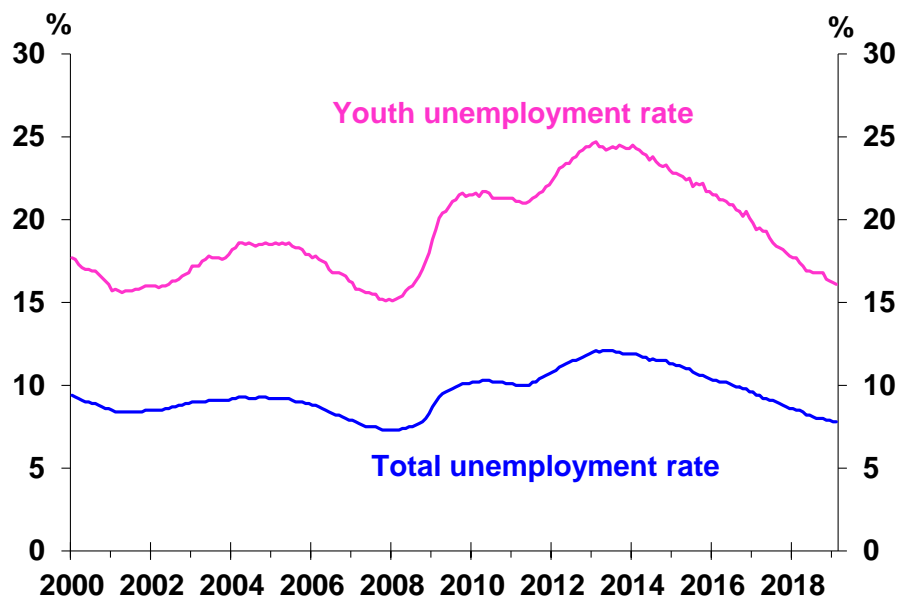
10-year sovereign bond yield



Note: 10-year Irish sovereign bond yield data is not available between 12 Oct 2011 and 14 Mar 2013
Source: Bloomberg



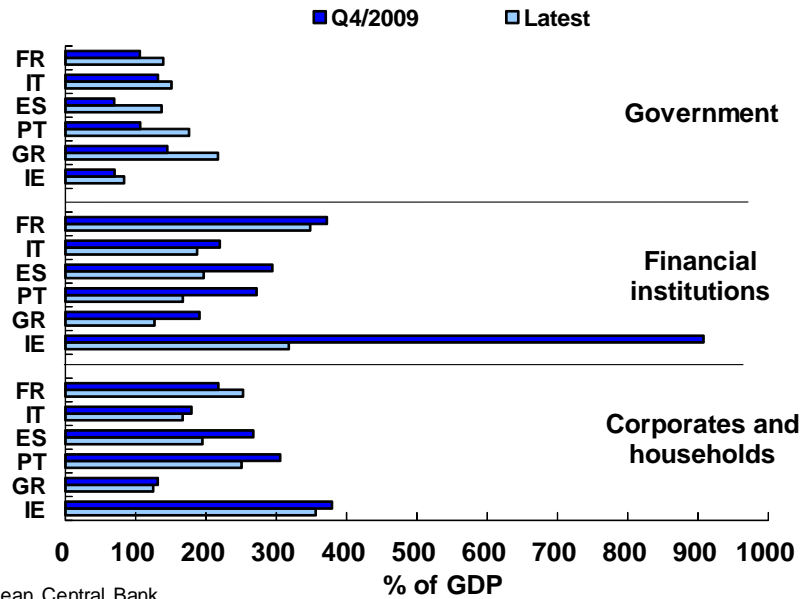
EURO AREA: UNEMPLOYMENT RATE



Source: Bloomberg



EURO AREA: OVERALL INDEBTEDNESS



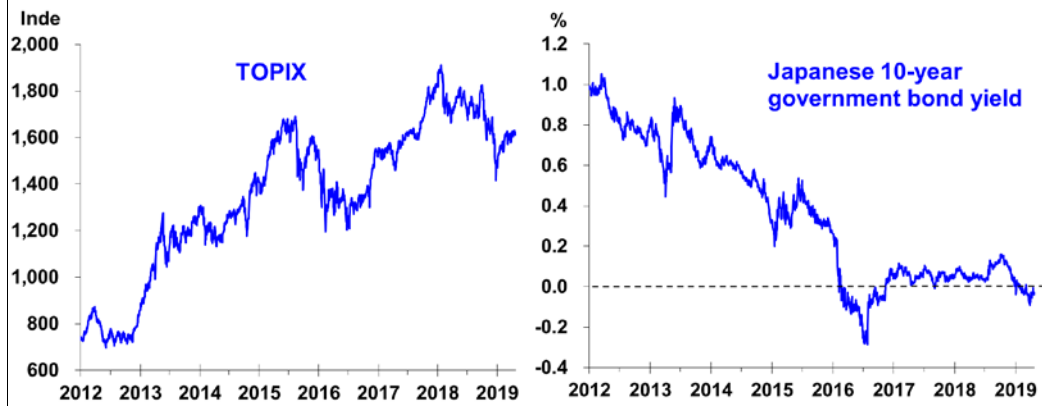
Source: European Central Bank

Note: FR – France, IT – Italy, ES – Spain, PT – Portugal, GR – Greece, IE – Ireland

The latest figures are up to Q4/2018 for financial institutions and corporates and households, and Q3/2018 for government



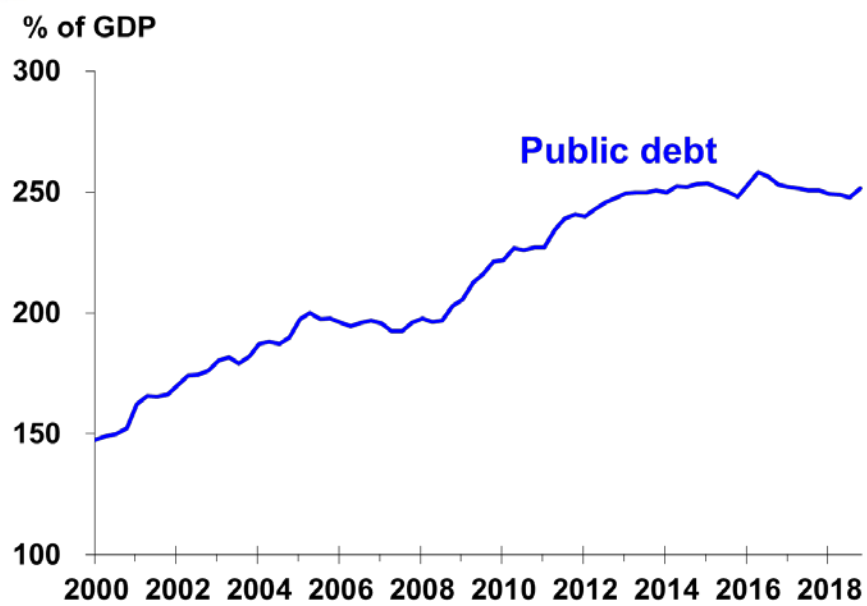
JAPAN: FINANCIAL MARKETS



Source: Bloomberg



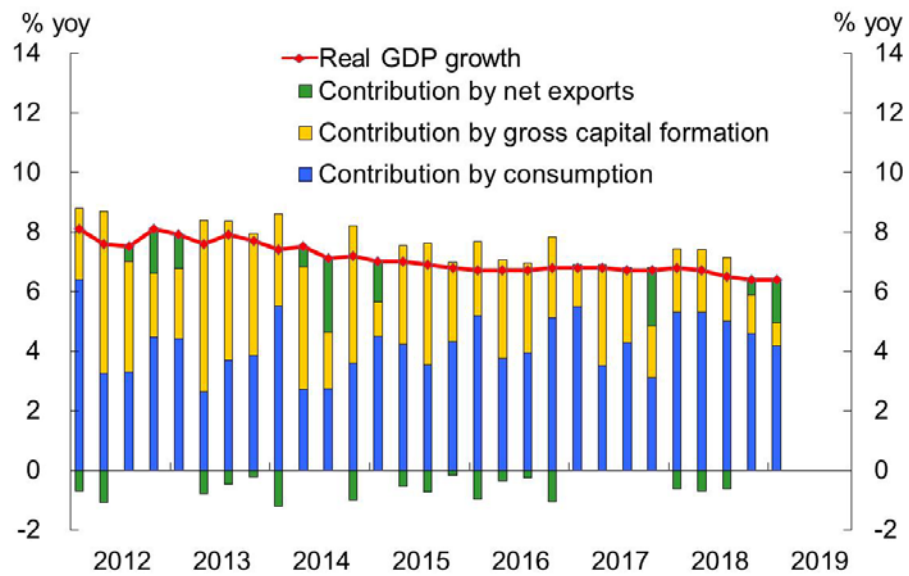
JAPAN: PUBLIC DEBT



Sources: Bank of Japan and CEIC



MAINLAND CHINA: REAL GDP GROWTH



Source: CEIC



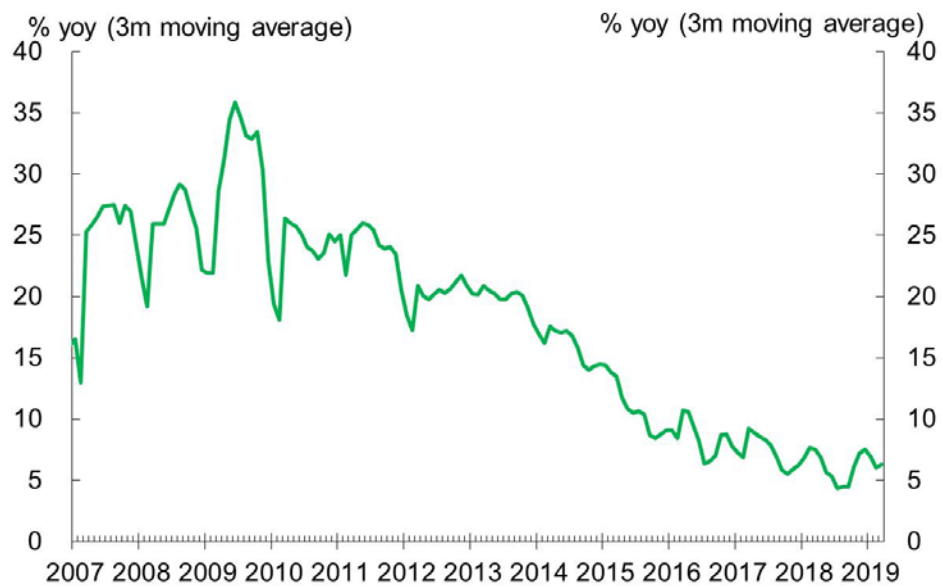
MAINLAND CHINA: RETAIL SALES



Note: January and February figures are the average annual growth rate for the first two months of the year
Sources: WIND and HKMA staff estimates



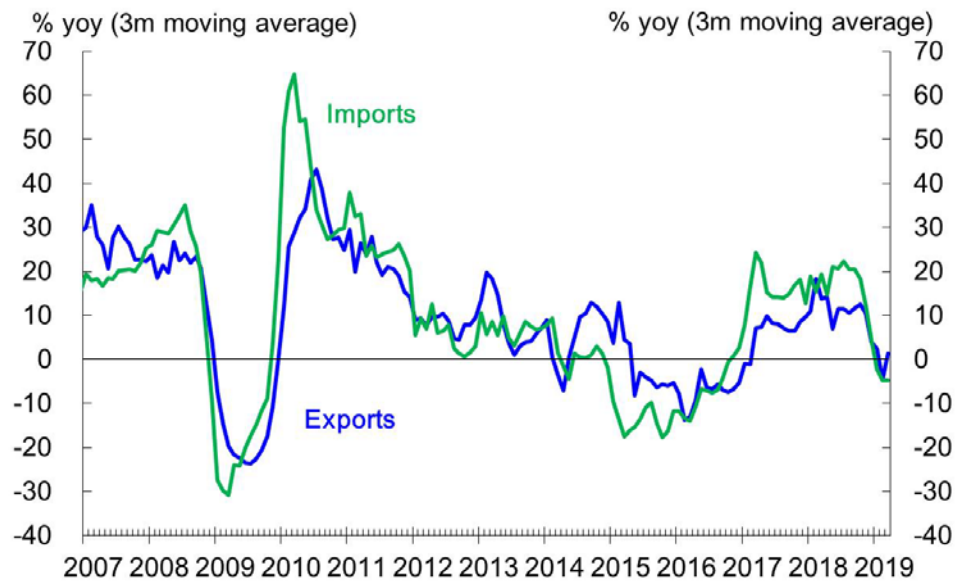
MAINLAND CHINA: FIXED ASSET INVESTMENT



Sources: CEIC and HKMA staff estimates



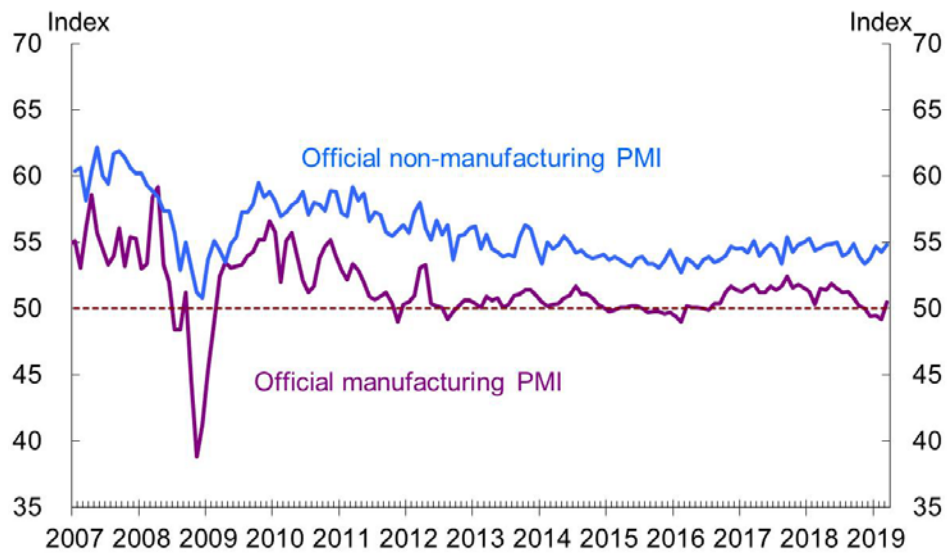
MAINLAND CHINA: IMPORT AND EXPORT GROWTH



Sources: CEIC and HKMA staff estimates



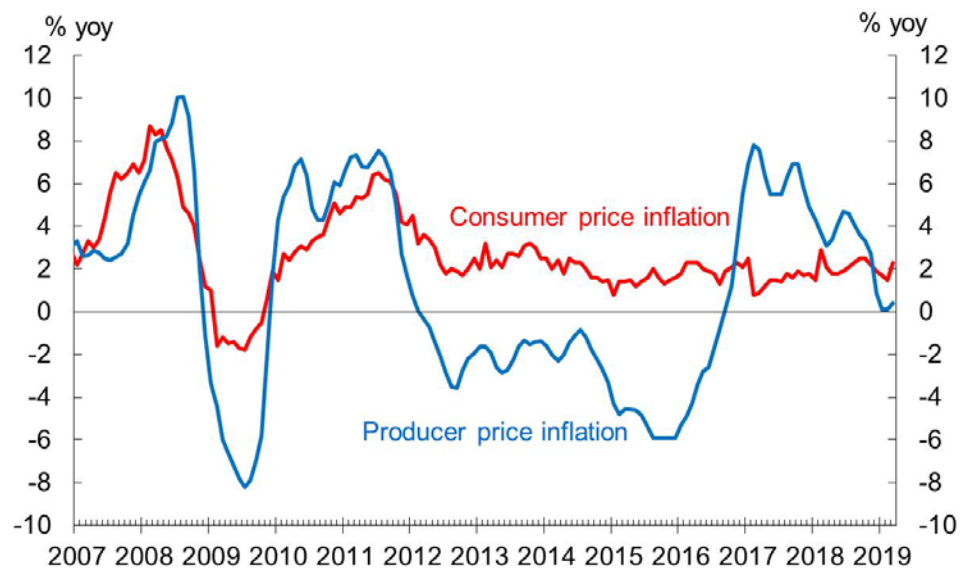
MAINLAND CHINA: PURCHASING MANAGERS' INDEX



Source: CEIC



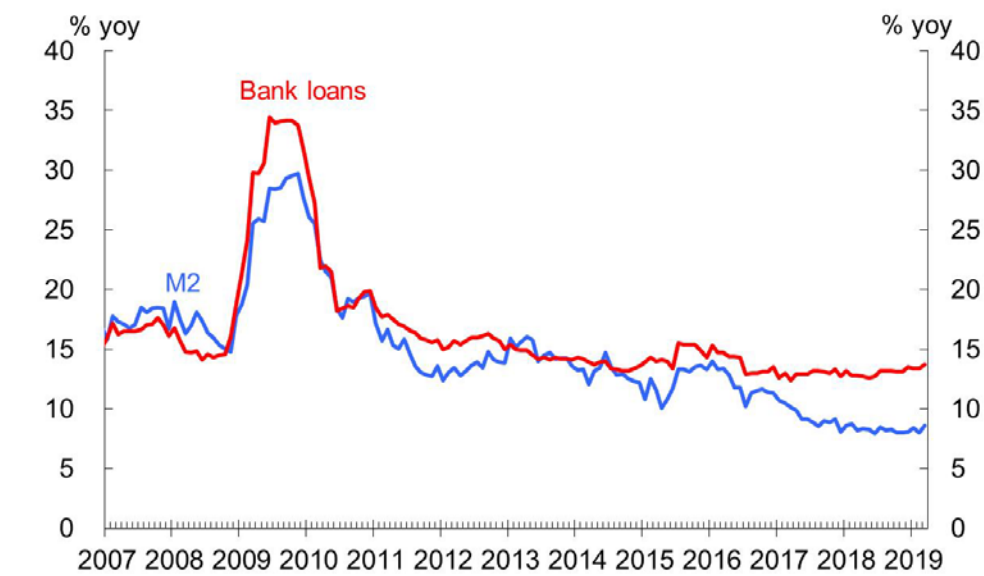
MAINLAND CHINA: INFLATION



Source: CEIC



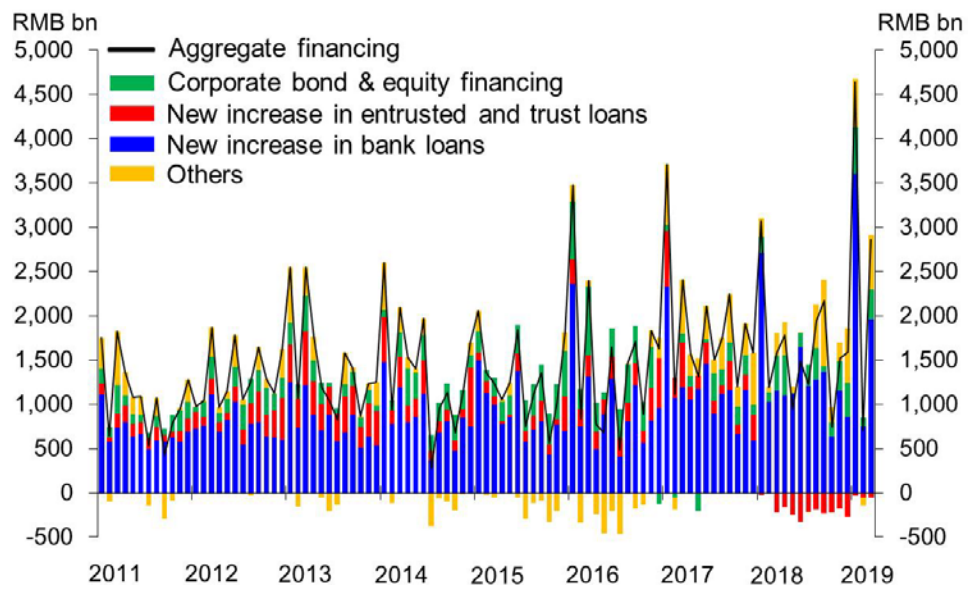
MAINLAND CHINA: MONEY AND LOAN GROWTH



Source: CEIC



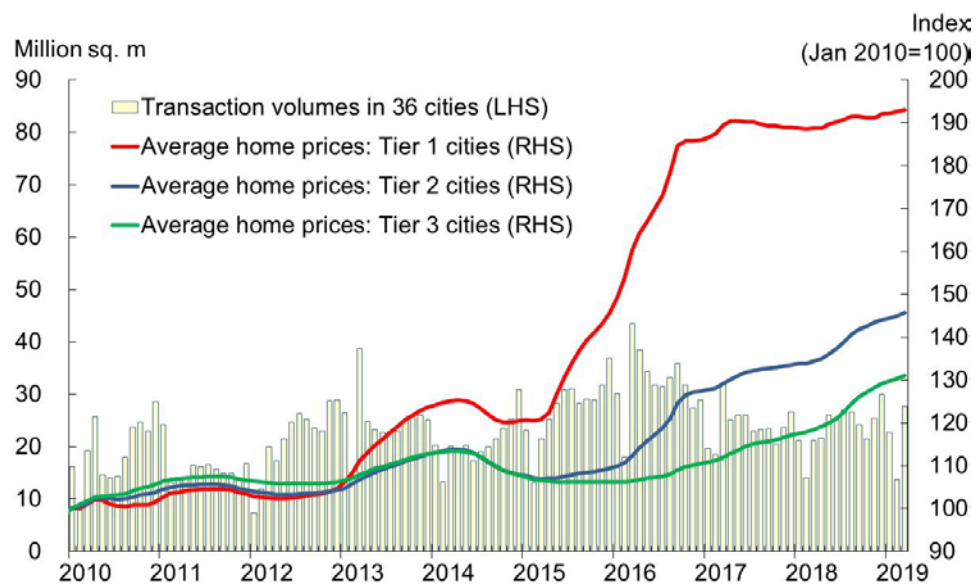
MAINLAND CHINA: AGGREGATE FINANCING FLOW



Source: CEIC



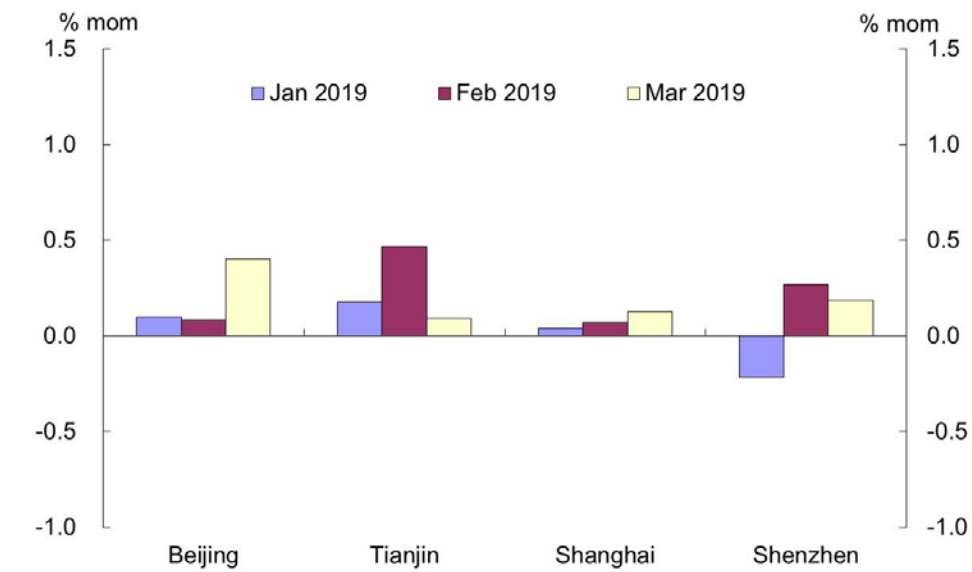
MAINLAND CHINA: PROPERTY PRICE AND TRANSACTION VOLUME



Sources: CEIC, WIND and HKMA staff estimates



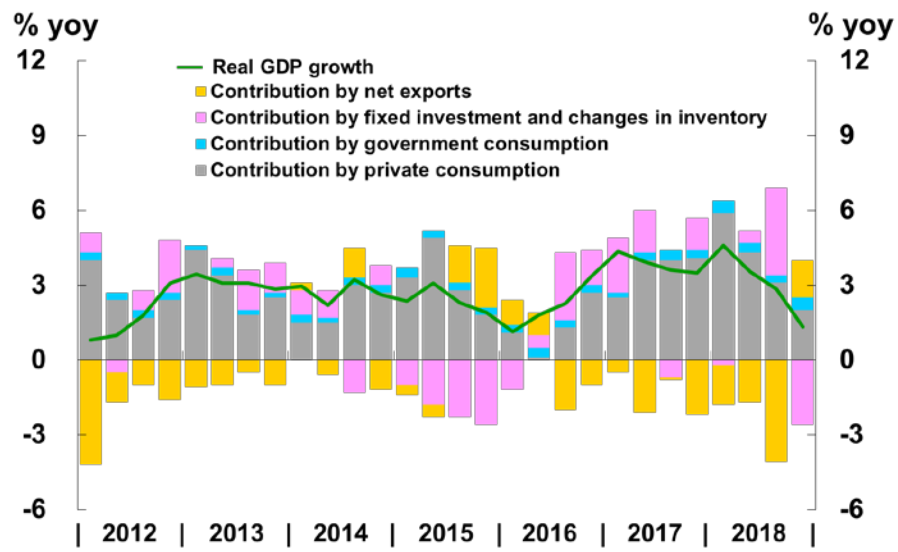
MAINLAND CHINA: HOUSING PRICE CHANGES IN MAJOR CITIES



Sources: CEIC, WIND and HKMA staff estimates



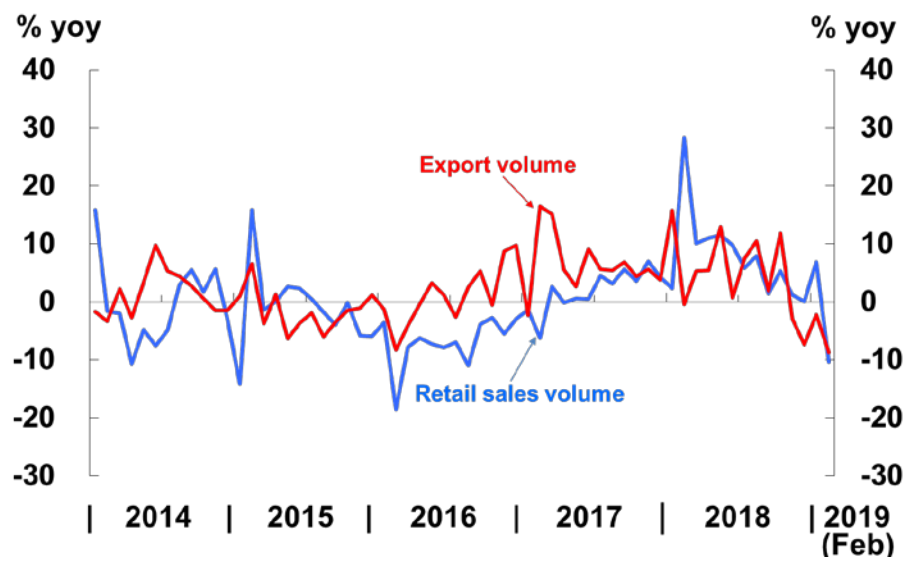
HONG KONG: REAL GDP GROWTH



Source: C&SD



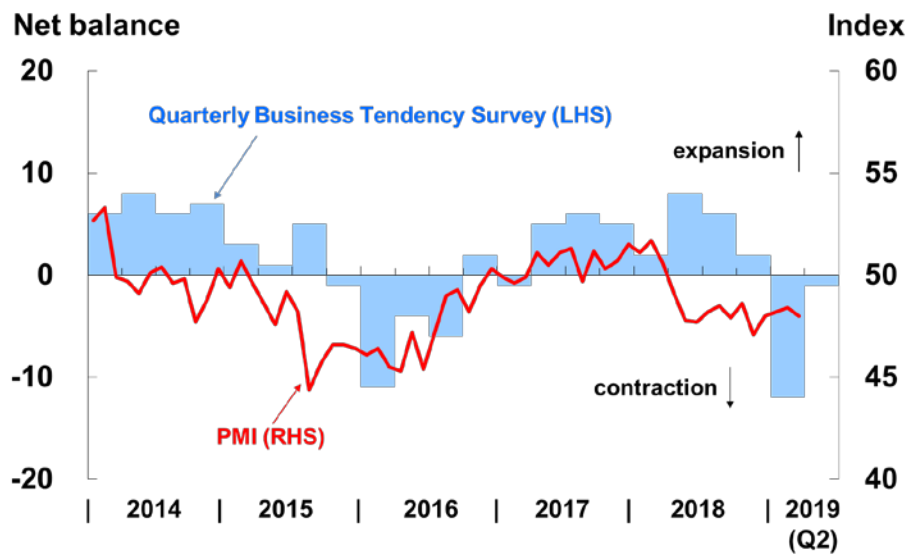
HONG KONG: ECONOMIC ACTIVITY



Source: C&SD



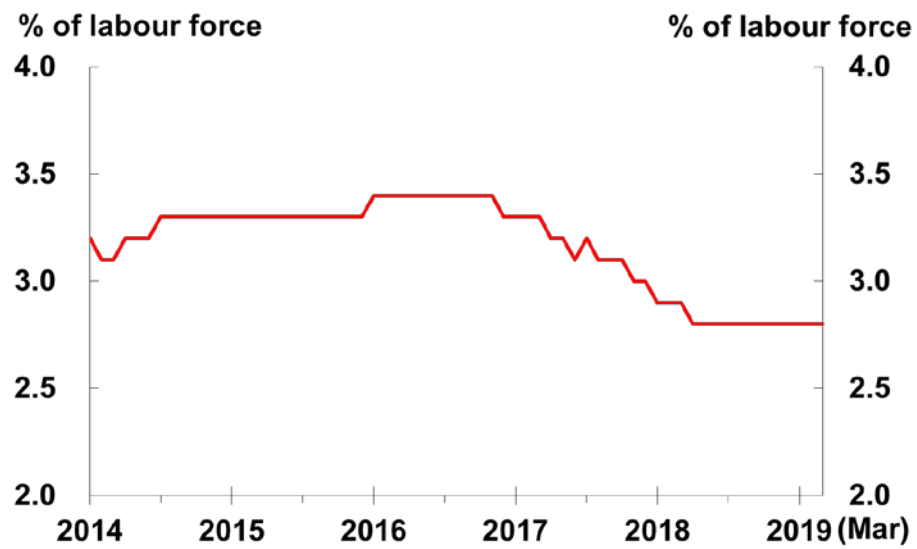
HONG KONG: BUSINESS OUTLOOK



Sources: C&SD and Markit



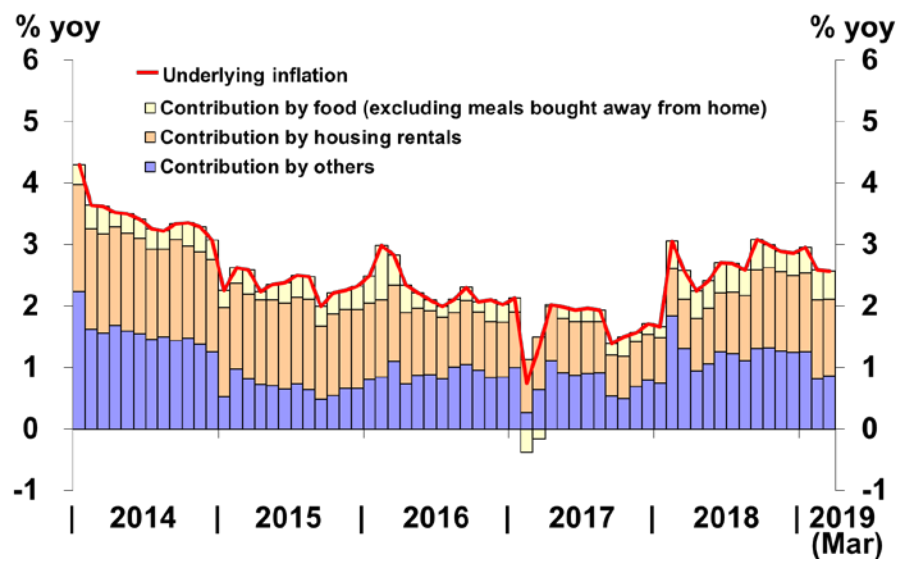
HONG KONG: UNEMPLOYMENT RATE



Source: C&SD



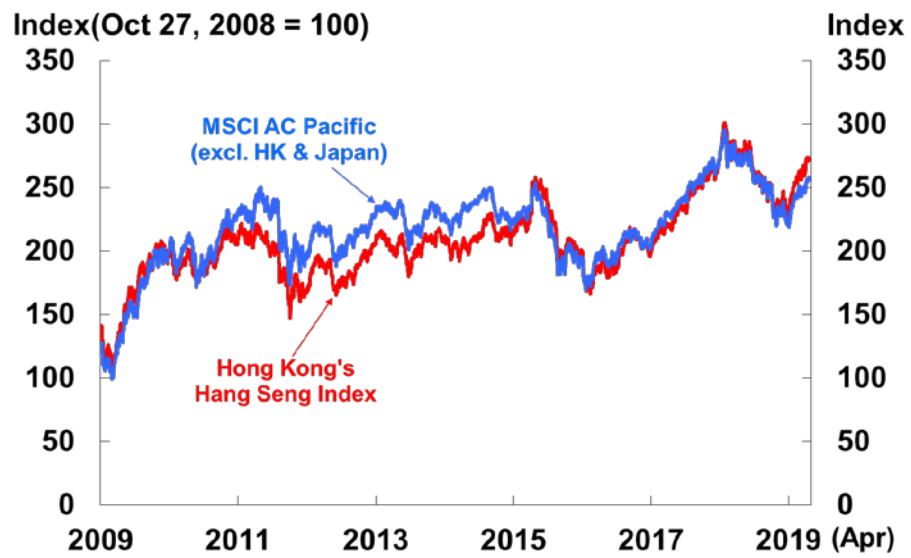
HONG KONG: INFLATION



Sources: C&SD and HKMA staff estimates



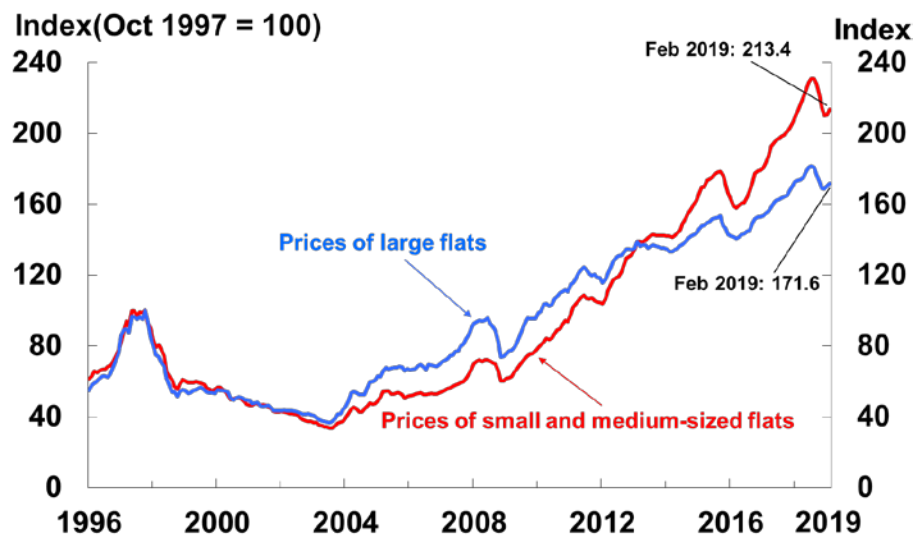
HONG KONG: EQUITY MARKET



Source: Bloomberg



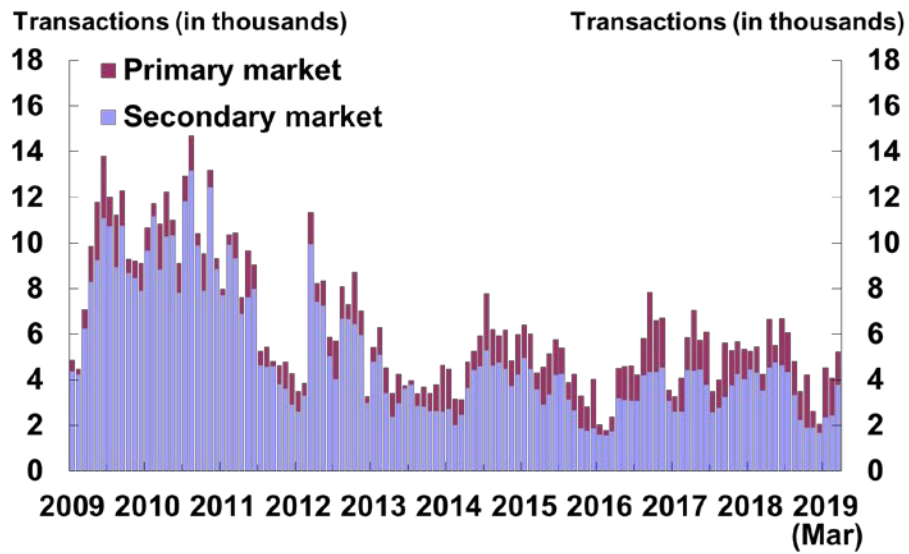
HONG KONG: RESIDENTIAL PROPERTY PRICES



Source: Rating and Valuation Department



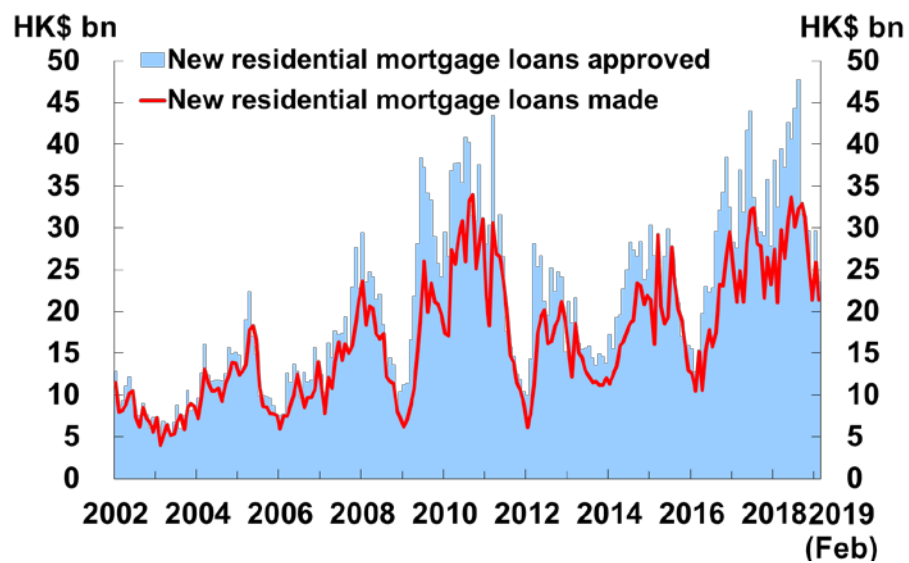
HONG KONG: TRANSACTION VOLUME IN THE PRIMARY AND SECONDARY MARKETS



Source: The Land Registry



HONG KONG: NEW RESIDENTIAL MORTGAGE LOANS

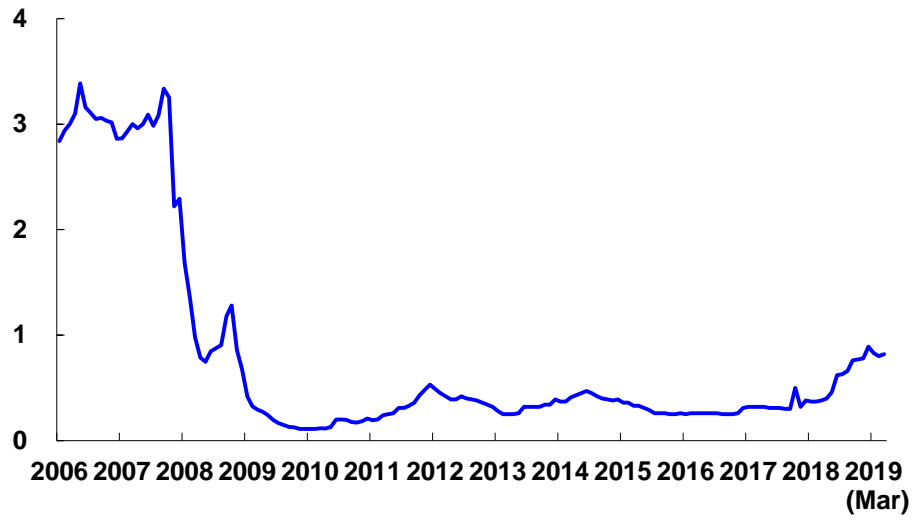


Source: HKMA



HONG KONG: COMPOSITE INTEREST RATE

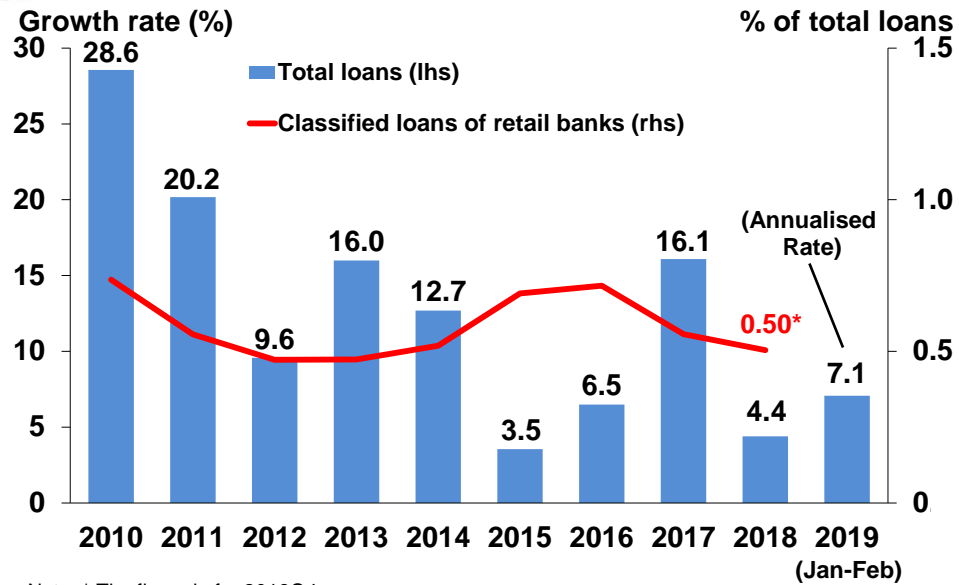
% p.a.



Source: HKMA



HONG KONG: LOAN GROWTH AND ASSET QUALITY

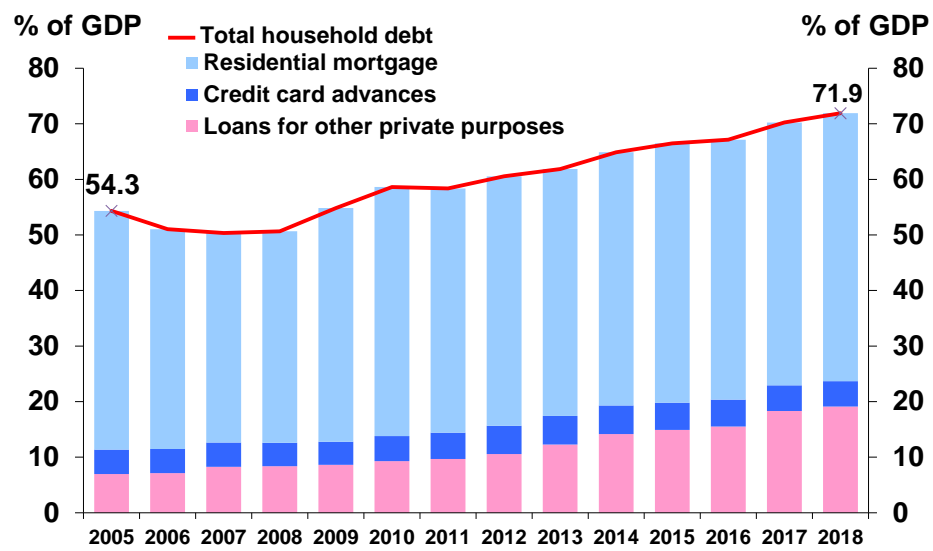


Note: * The figure is for 2018Q4.

Source: HKMA



HONG KONG: HOUSEHOLD DEBT



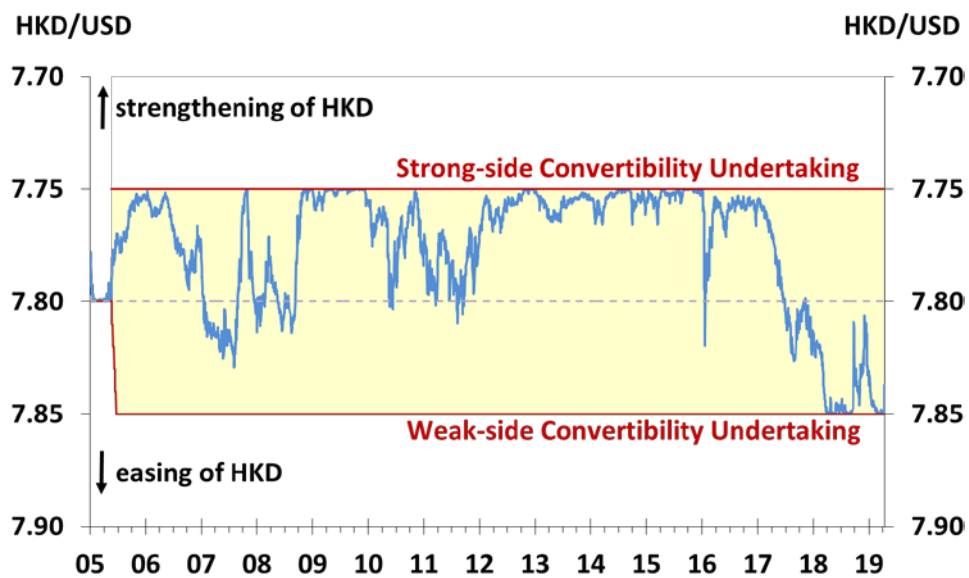
Source: HKMA



CURRENCY STABILITY



HONG KONG DOLLAR SPOT EXCHANGE RATE

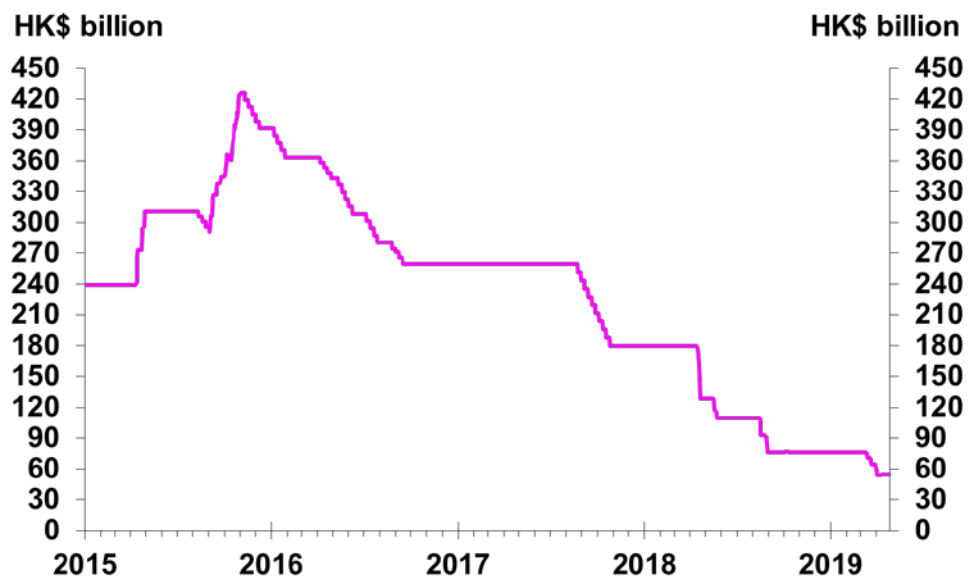


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- The weak-side Convertibility Undertaking was triggered eight times in March 2019.



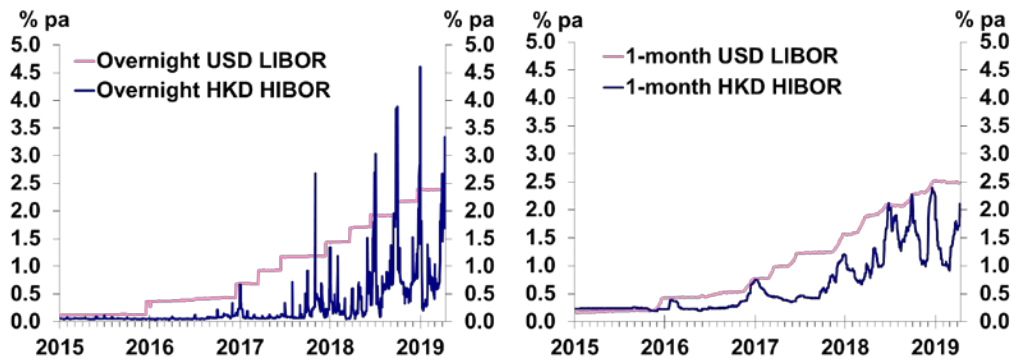
AGGREGATE BALANCE



- The Aggregate Balance stood at HK\$54.4 billion.



DOMESTIC INTEREST RATES





12-MONTH HONG KONG DOLLAR FORWARD POINTS



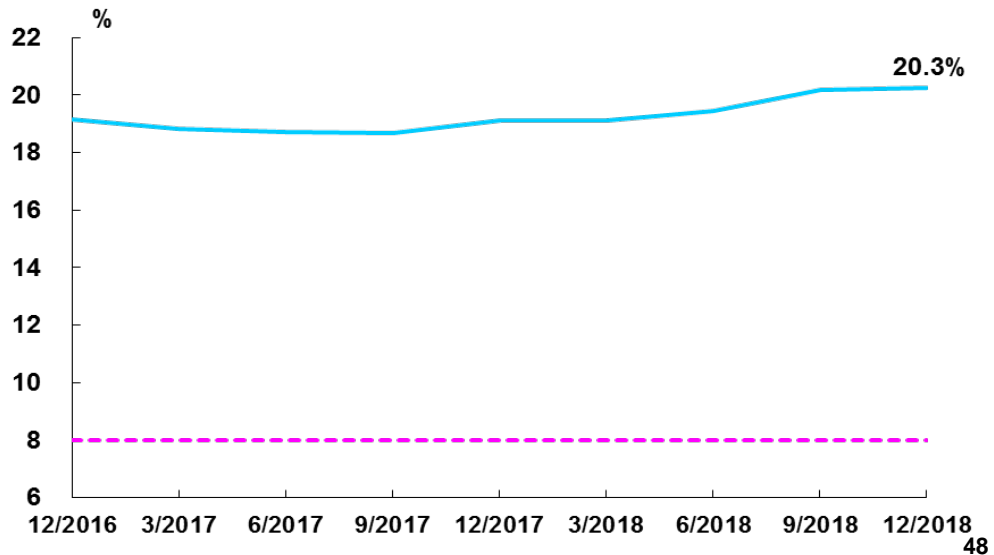


BANKING STABILITY



BANKING SECTOR PERFORMANCE

Locally incorporated authorized institutions (AIs)
remained well capitalised

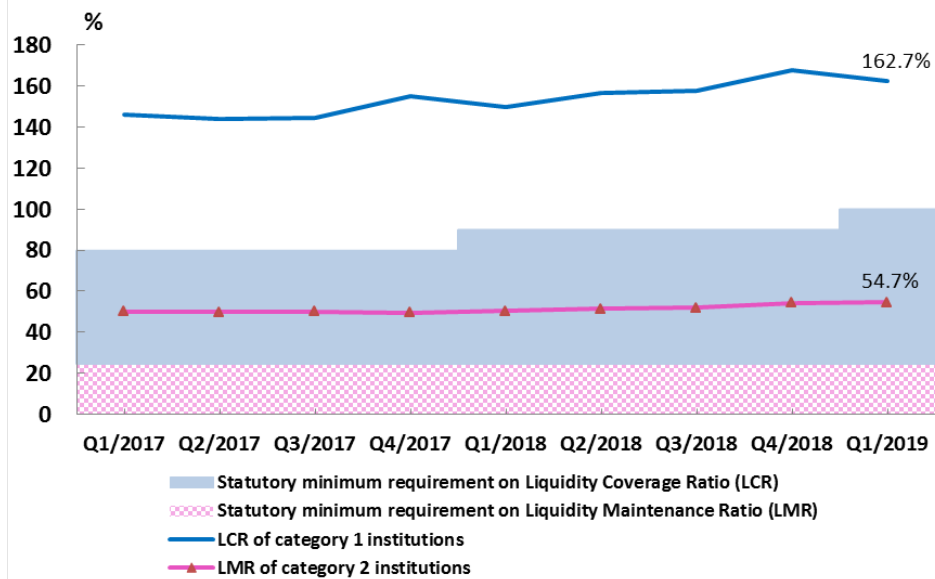


- The banking sector continued to be well capitalised. The consolidated capital adequacy ratio of locally incorporated AIs stood at 20.3% at end-December 2018, well above the international minimum requirement of 8%.



BANKING SECTOR PERFORMANCE

Liquidity position continued to be sound



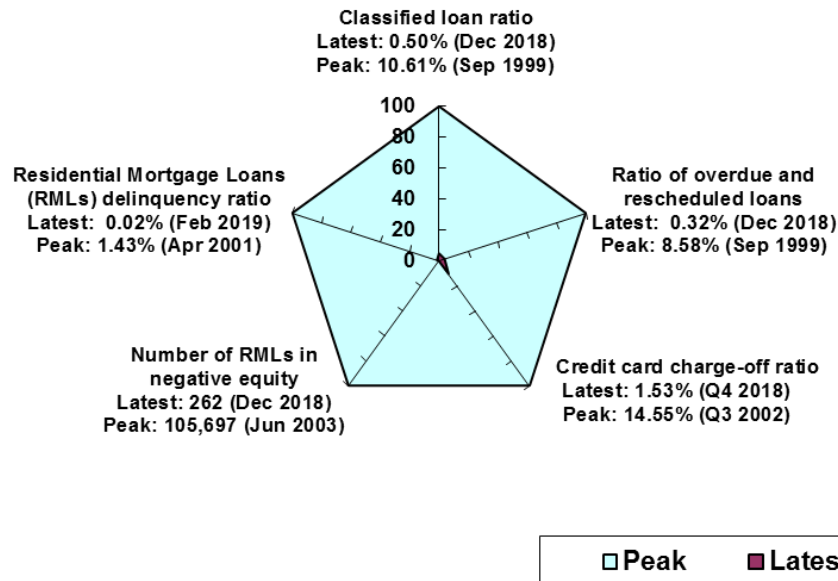
49

- In the first quarter of 2019, the quarterly average LCR of category 1 institutions was 162.7%, well above the 100% statutory minimum requirement applicable for 2019. For category 2 institutions, their quarterly average LMR was 54.7%, also well above the 25% statutory minimum requirement.



BANKING SECTOR PERFORMANCE

Asset quality remained good



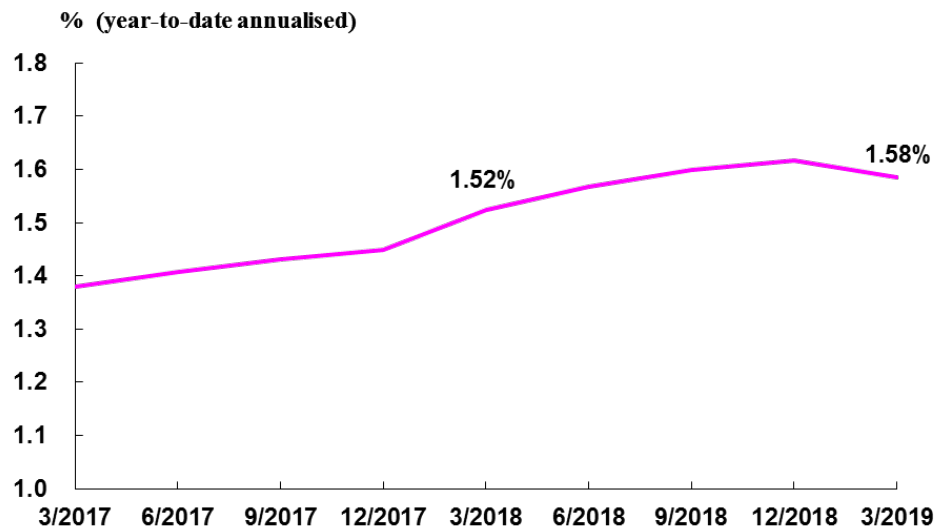
50

- The asset quality of retail banks remained good. Their classified loan ratio decreased to 0.50% at end-December 2018 from 0.54% a quarter earlier, well below the long-run historical average of 2.1% since 2000. For the banking sector as a whole, the classified loan ratio also reduced to 0.55% from 0.60% during the same period.



BANKING SECTOR PERFORMANCE

Net interest margin widened



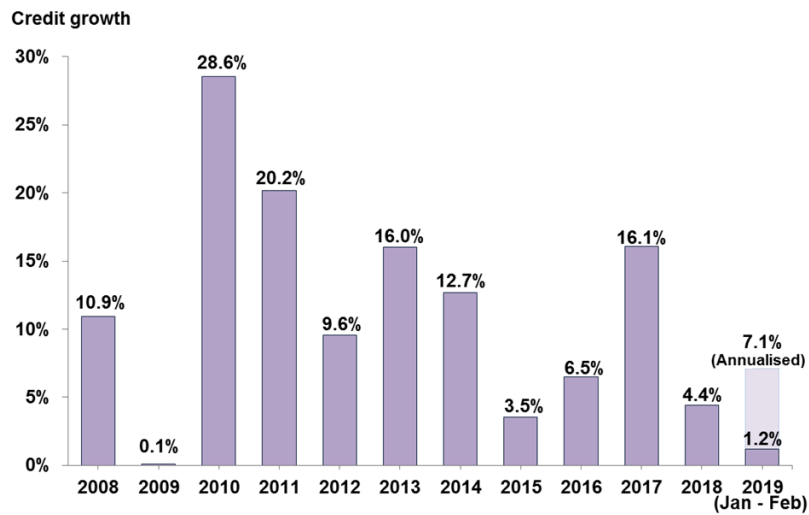
51

- The net interest margin of retail banks' Hong Kong offices widened to 1.58% in the first quarter of 2019 from 1.52% in the same period last year.



BANKING SECTOR PERFORMANCE

Credit grew at a moderate pace



Source: HKMA

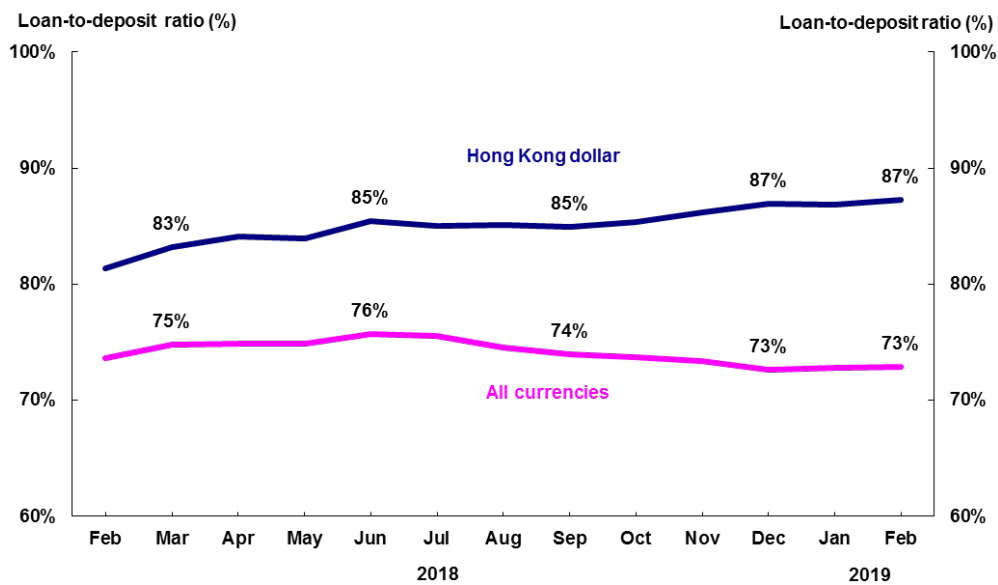
52

- Credit grew moderately amid uncertain global economic and trade environment. Total loans increased by 1.2% in the first two months of 2019.



BANKING SECTOR PERFORMANCE

Loan-to-deposit ratios were broadly stable



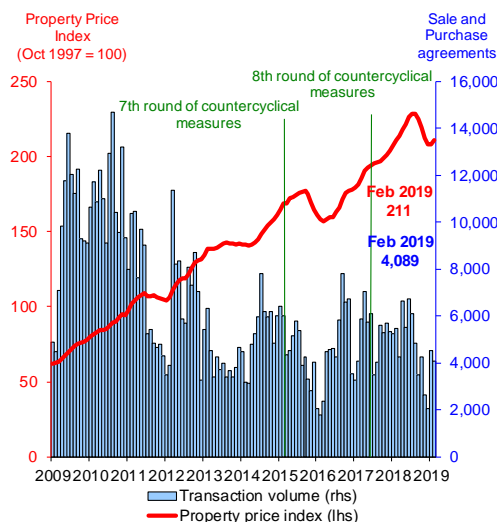
53

- Hong Kong-dollar loan-to-deposit ratio stood at 87% at end-February 2019, same as that at end-December 2018.
- All currencies loan-to-deposit ratio remained steady at 73% at end-February 2019.



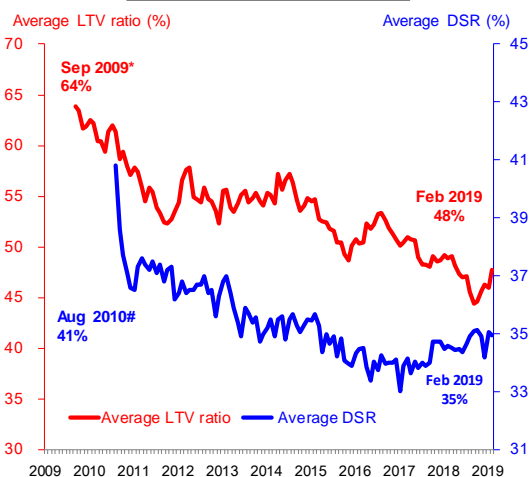
PROPERTY MORTGAGE LOANS

Residential property price index and transaction volume



Sources: R&VD and Land Registry

Average loan-to-value (LTV) ratio and debt servicing ratio (DSR) for new residential mortgage loans approved



* Before the first round of HKMA's countercyclical measures was introduced

When the tighter requirement on debt servicing ratio was introduced by the HKMA

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Latest statistics on residential mortgage loans (RMLs)

	Monthly average in 2017	Monthly average in 2018	Sep 2018	Oct 2018	Nov 2018	Dec 2018	Jan 2019	Feb 2019
Number of sale and purchase agreements	5,133	4,771	3,500	4,243	2,635	2,060	4,543	4,089
Number of new RML applications	11,947	12,567	7,977	10,754	9,431	7,435	11,496	10,133
Number of new RMLs approved	8,699	9,010	7,712	7,417	7,341	5,699	6,963	6,422

Latest statistics on residential property prices

Property price index		Period	Property price index
Rating and Valuation Department (10/1997=100)	Latest position	2/2019	211.2
	Recent peak	7/2018	228.3
	Peak in 1997	10/1997	100.0
Centaline (6/7/1997=100)	Latest position	24/3/2019	177.4
	Recent peak	12/8/2018	188.6
	Peak in 1997	19/10/1997	102.9



INTERNATIONAL STANDARDS IMPLEMENTATION

- Banking (Liquidity) (Amendment) Rules 2019
- Banking (Capital) (Amendment) Rules 2019 / 2020

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The following legislative proposals are being prepared for the purpose of implementing the Basel regulatory standards:

Liquidity standards

- We are preparing to introduce a set of Banking (Liquidity) (Amendment) Rules 2019 to accept Basel III-compliant listed equities and triple-B rated debt securities as high quality liquid assets under the “level 2B assets” class for the Liquidity Coverage Ratio. We will also follow the latest Basel guidance to implement a 5% “required stable funding” requirement for derivative liabilities under the Net Stable Funding Ratio. We plan to implement these amendments from 1 January 2020.

Capital standards

- Meanwhile, we are in the process of preparing a set of Banking (Capital) (Amendment) Rules, mainly to incorporate the following three Basel capital standards:
 - the standard on banks’ equity investments in funds;
 - the standardised approach for measuring counterparty credit risk of derivative contracts (SA-CCR); and
 - the final standard on banks’ exposures to central counterparties (in centrally-cleared transactions), replacing the interim standard that has been in effect in Hong Kong since 2013.
- Industry consultation on the proposed provisions for implementation of the standards are being conducted in stages. The amendment rules are currently targeted to be submitted to the Legislative Council towards the

end of 2019 or during the first half of 2020, in order for the standards to take effect in Hong Kong within 2020. (Note: These standards were originally scheduled to be effective on 1 January 2017 according to the Basel timeline. Local implementation has been deferred to track more closely the implementation schedules in other major jurisdictions.)



RESOLUTION REGIME

- The Inland Revenue (Amendment) Ordinance 2019 commenced operation on 15 February 2019
- The finalised Financial Institutions (Resolution) Ordinance (FIRO) code of practice chapter in relation to the Financial Institutions (Resolution) (Loss-absorbing Capacity Requirements – Banking Sector) Rules (LAC Rules) was published on 20 March 2019
- Continue to operationalise the FIRO by progressing other secondary legislation

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- Following the coming into operation on 14 December 2018 of the LAC Rules, the Inland Revenue (Amendment) Ordinance 2019, which clarifies the tax treatments for instruments issued by Als to meet the requirements under the LAC Rules, commenced operation on 15 February 2019. Following the amendment, non-capital loss-absorbing capacity (LAC) debt instruments will receive debt-like tax treatment. This follows the amendment in 2016 (by way of the Inland Revenue (Amendment) (No. 2) Ordinance 2016) to allow Additional Tier 1 and Tier 2 capital instruments (i.e. capital LAC debt instruments) to receive debt-like tax treatment.
- The finalised FIRO code of practice chapter in relation to the LAC Rules was published on 20 March 2019. Feedback from the industry consultation has been reflected as appropriate.
- On other subsidiary legislation to be made to operationalise FIRO, the HKMA plans to consult, in the first half of 2019, on policy proposals for imposing contractual requirements on Als under section 92 of the FIRO regarding stays on early termination rights of financial contract.



FINANCIAL INCLUSION

Banking services delivery channels

- More physical branches for underserved areas

Bank account opening and maintenance

- Encourage banks to launch Simple Bank Accounts (SBAs) with less extensive customer due diligence measures to facilitate access to banking services by corporates and enhance customer experience
- Mystery shopping programme (MSP) and thematic reviews
- Exploring the use of new technology to enhance efficiency of customer due diligence process

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- The HKMA has been following up and coordinating with retail banks to further enhance the coverage of banking networks in remote areas and public housing estates. Positive responses were received from banks, with a new branch set up in a public housing estate in Kwun Tong at the beginning of the year and additional branches expected in two other public housing estates in the next six months or so to further enhance banking services in the areas.
- The HKMA has been exploring with banks the introduction of measures to facilitate access to banking services by businesses and the general public and to enhance customer experience. With the encouragement of the HKMA, some banks have launched SBA service to provide basic banking services with less extensive customer due diligence measures to eligible corporate customers based on their actual business needs. SBA customers that require more comprehensive banking services in the future may upgrade their accounts to traditional bank accounts by completing the necessary customer due diligence process. Through the introduction of SBAs, the banking industry on one hand provides bank customers with the option of another type of bank accounts, and on the other hand also addresses the needs of corporate customers at different stages. The HKMA issued a circular to AIs in April to encourage more banks to support and launch SBAs to provide corporate customers with more choices.
- On bank account opening, the service provider engaged by the HKMA for the MSP has completed the on-site fieldwork at retail banks. The HKMA is analysing the review results and working on a circular to share the MSP observations with the industry.

- The Anti-Money Laundering and Counter-Terrorist Financing (Financial Institutions) (Amendment) Ordinance 2018 became effective last year, allowing greater flexibility for banks to remotely process account opening and update customers' information. The HKMA has been maintaining close dialogues with banks and fintech companies on their initiatives through the Fintech Supervisory Sandbox and Chatroom. Recently, the HKMA also articulated to the industry regarding the principles of identity authentication and identity matching when opening account remotely for individual customers, and reminded banks to adopt a risk-based approach during the processes of account opening and maintenance. Meanwhile, the HKMA is working with the Hong Kong Association of Banks to explore how technology, including a know-your-customer utility, can potentially be used to enhance efficiency of customer due diligence processes and customer experience.



BANKING CONSUMER PROTECTION

- Worked closely with the Hong Kong Association of Banks (HKAB) in developing a set of standardised procedures for the industry to handle cases of mis-transfer of funds erroneously made by customers
- Working closely with HKAB to follow up with TransUnion (TU) in respect of security loopholes in its online consumer credit report service

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- **Mis-transfer of Funds Made by Customers:** Regarding the situation where bank customers erroneously transfer funds to wrong recipients and request assistance from their banks to recover the mis-transferred funds, the HKMA requested the banking industry to look into the matter and seek to further enhance banks' existing process. HKAB, in consultation with the HKMA, has worked out a set of standardised procedures to provide greater clarity and further enhancement to banks' existing processes. The HKMA has issued a circular in January 2019 to remind banks to have a proper process for ensuring that the aforementioned procedures are duly adopted and enforced. The procedures have been effective starting from 25 March 2019.
- **TransUnion incident:** The HKMA continues to work closely with HKAB in following up with TU on their remediation actions and enhanced controls. The HKMA will also make reference to the results of the investigation being conducted by the Office of the Privacy Commissioner for Personal Data, and work with the banking industry to review the contractual arrangement between the industry and credit reference agency, with a view to strengthening the current arrangement.



BANKING INVESTOR PROTECTION

- Working with Insurance Authority (IA) to implement the new statutory regime for regulating insurance intermediaries
- Issued guidance to banking industry on selling of Qualifying Deferred Annuity Policy (QDAP) to ensure Als' compliance with relevant regulatory requirements

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- The HKMA continued to work with the IA to prepare for the implementation of the statutory regime under the new Insurance Ordinance for regulating insurance intermediaries, including a collaboration framework for inspection and investigation of insurance intermediary activities of Als, and formulation of rules and regulatory requirements for the new regime.
- The HKMA issued guidance on the selling of QDAP to the banking industry to ensure Als' compliance with relevant regulatory requirements. This circular draws Als' attention to the Guideline on Qualifying Deferred Annuity Policy (i.e. GL19) recently issued by the IA and highlights the information that should be disclosed and explained to customers during the selling process of QDAPs.



VIRTUAL BANKING

- The HKMA has granted four virtual banking licences by end-April and is making good progress in the processing of the remaining four virtual bank applications which have been shortlisted for detailed due diligence
- According to the business plans submitted by the applicants, virtual banking services are expected to be launched within six to nine months after a licence is granted
- Applicants are required to complete a range of preparatory work to meet supervisory expectations before commencing business

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Preparations prior to commencement of business include:

- Testing of IT platform and system;
- Finalisation of detailed risk management measures and controls;
- Setting up remote account opening procedures & AML/CFT controls; and
- Human resources.



ENHANCED COMPETENCY FRAMEWORK (ECF) FOR BANKING PRACTITIONERS

- Launched the ECF module on credit risk management in March 2019 for capacity building and talent development of practitioners
- Commenced preparatory work on the development of the ECF module on risk management and compliance

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- With the support of the banking industry and relevant professional bodies, the HKMA launched the ECF module on credit risk management in March 2019 for enhancing capacity building and talent development in the professional areas of commercial lending and credit risk management. Banking practitioners can develop their professional competence in a more structured manner.
- The HKMA will continue to collaborate with the relevant parties regarding the preparatory work on the development of the ECF on risk management and compliance.



PUBLIC EDUCATION

- Kicked off a new phase of the Cross Generation Outreaching Educational Programme
- Further promoted smart use of credit cards and understanding of credit card chargeback protection



Snapshots of the kick-off ceremony of the second phase of the Cross Generation Outreaching Educational Programme

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- The HKMA organises the Cross Generation Outreaching Educational Programme jointly with the Hong Kong Institute of Vocational Education. The Programme aims at disseminating different levels of money management concepts and smart use of banking and financial services to kindergarten students and their parents, teachers of participating kindergartens, as well as teenagers. An achievement ceremony for the first phase was held recently and the launch of the second phase was announced.
- The HKMA also arranged further publicity to promote smart use of credit cards and enhance the public awareness and understanding of the credit card chargeback protection.



DEPOSIT PROTECTION SCHEME (DPS)

- Adopting electronic payment channels for paying compensation to depositors:
 - Conducted feasibility study and cost & benefit analysis;
 - To commence the project for implementation
- Reinforcing public awareness of the DPS:
Launched a multi-media publicity campaign and “My Piggy Bank Roving Art Installation”



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- Preparatory work is in progress for the project to implement electronic payment channels for paying compensation to depositors.
- Launched initiatives to promote awareness and understanding of the DPS:
 - a multi-media publicity campaign in January 2019 with a series of new advertisements featuring animated piggy-bank characters designed by three local illustrators; and
 - “My Piggy Bank Roving Art Installation” during the Chinese New Year, displaying 66 piggy-bank art pieces designed by primary school, secondary school and college students as well as local artists, together with information panels, interactive workshops and drama sessions.



ACADEMY OF FINANCE (AoF)

- The preparatory work for establishing the Academy of Finance is progressing well. The AoF is expected to be launched in late June.



FINANCIAL INFRASTRUCTURE



FINANCIAL INFRASTRUCTURE

- Financial infrastructure remains safe and efficient
- Operation of Bond Connect has been smooth; actively promote Bond Connect to overseas investors
- Further refine the over-the-counter derivatives trade repository (TR) according to the relevant local and international standards

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Bond Connect

- Since the launch of Bond Connect on 3 July 2017, related settlement operations performed by the Central Moneymarkets Unit has been smooth.
- With the Delivery-versus-Payment settlement fully implemented in August 2018, and the inclusion of CNY denominated Chinese government and policy bank securities into the Bloomberg Barclays Global Aggregate Index as scheduled in April 2019, more and more overseas investors have started to invest into the China interbank bond market via Bond Connect. The HKMA has been maintaining close communication with the People's Bank of China and relevant Mainland institutions to explore enhancements to Northbound Trading.

Over-the-counter derivatives trade repository

- Since the reporting function of the TR was launched in July 2013, reporting by banks to the TR has been smooth.



FASTER PAYMENT SYSTEM (FPS)

- FPS adoption continued to grow. As of 31 March 2019:
 - Registrations: 2.6 million
 - Transaction value: HK\$226 billion
 - Transaction number: 11 million
 - Average daily transaction value: HK\$1.2 billion
 - Average daily transaction number: 61,000

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- Currently, a total of 21 banks (including most retail banks) and 10 stored value facilities (SVFs) in Hong Kong have participated in the system to provide FPS services for their customers.
- FPS has received a total of 2.59 million registrations, including 1.79 million in mobile numbers, 430,000 in email addresses, and 370,000 in FPS ID as of 31 March 2019.
- FPS has processed 11 million transactions with transaction amount totalling over HK\$226 billion and RMB6 billion as of 31 March 2019.
- At present, the usage is mainly on person-to-person payments and it is expected that more business transactions will be conducted through the system going forward.
- Banks and SVFs are currently focusing on improving their funds transfer services through online banking, mobile banking or e-wallet. They will promote the use of FPS by merchants for collecting payments. It will take some time for merchants to understand the business benefits of adopting FPS and enhance their system functionalities for real-time payment collections.
- The Government is planning to adopt FPS to provide the public with greater convenience in paying taxes, rates and water charges. The Transport Department, the Immigration Department and the Leisure and Cultural Services Department will examine the feasibility of accepting payments through the FPS at their shroff counters on a pilot basis.



LATEST FINTECH INITIATIVES

Open Application Programming Interface (Open API) for the banking industry

- Over 300 registrations from third-party service providers were recorded to access banks' Phase I Open APIs
- Phase II implementation underway

Global Financial Innovation Network (GFIN)

- The HKMA is a founding member of GFIN, which was launched in January 2019
- Processing about 20 applications for cross-border testing of fintech products

Fintech Career Accelerator Scheme 2.0

- 175 gap year placement positions to be offered by 18 banks and three stored value facility operators

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Open API for the banking industry

- Phase II - Banks will launch Open APIs to support applications for banking products and services in October 2019.

Global Financial Innovation Network (GFIN)

- GFIN is an international network of 29 organisations committed to supporting financial innovation in the interests of consumers.
- Together with other members, the HKMA invited applications from firms wishing to test innovative financial products, services or business models across more than one jurisdiction.
- The HKMA received applications from jurisdictions including the UK and the US.



STORED VALUE FACILITIES (SVFs) AND RETAIL PAYMENT SYSTEMS (RPSs)

- SVF usage continued to grow in Q4 2018:
 - Accounts in use: 56.1 million (+20.1% year-on-year (yoy))
 - Average daily transaction number: 17.8 million (+9.7% yoy)
 - Average daily transaction value: HK\$523 million (+24.4% yoy)
- SVF licensees continue to extend their business reach, e.g. cross-border remittance and retail payments, public transport and small merchants
- SVF Security 2.0
 - Enhancements in SVF account structure and account opening
 - Completed industry consultation and finalising way forward
- Continue to oversee six designated RPSs



REGULATORY DEVELOPMENT OF THE OVER-THE-COUNTER (OTC) DERIVATIVES MARKET

- Following public consultation, the subsidiary legislation to expand the mandatory clearing obligation was tabled before LegCo in December 2018 for operation in March 2019
- As of end of March 2019, the Hong Kong Trade Repository logged 2.67 million total outstanding OTC derivatives trades which covered five asset classes under mandatory reporting requirements, i.e. foreign exchange, interest rate, equity, credit and commodity derivatives

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Further enhancement to the OTC Derivatives Regulatory Regime

- Following the enactment of the Securities and Futures (Amendment) Ordinance 2014, which provides for the regulatory regime for the OTC derivatives market, we continue to develop specific regulatory requirements covering different aspects.
- A joint consultation conclusion paper with the Securities and Futures Commission, summarising the new requirements on the use of Legal Entity Identifier for reporting obligations, an expanded clearing obligation and the trading determination process, was published in June 2018. The subsidiary legislation for expanding mandatory clearing obligation was tabled before LegCo for negative vetting in December 2018 and took effect from 1 March 2019.



INTEREST RATE BENCHMARKS

- Continue to work with the Treasury Markets Association (TMA) on development of an alternative reference rate for HIBOR. TMA has proposed Hong Kong Dollar Overnight Index Average (HONIA) as the alternative rate, and is also conducting a consultation with the industry on some technical refinements to HONIA
- TMA will also engage the industry on promoting the use of HONIA in their day-to-day transactions
- Continue to closely monitor benchmark reforms in other major jurisdictions, in particular possible discontinuation of LIBOR after end-2021. The HKMA issued a letter to banks in March reminding them to start early assessment of risks and implications on their operation arising from the reforms, and develop plans to ensure a smooth transition



CURRENCY

- 2018 New Series Banknotes — the three note-issuing banks' new \$1000 and \$500 notes are already in circulation, and the remaining three denominations will enter circulation by phases between mid-2019 and 2020
- Two “Coin Carts” will continue to collect coins from members of the public in 18 districts
- Collaborated with Big Waster to jointly promote the use of good-as-new banknotes for lai-see in Chinese New Year



Cross-over with Big Waster

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2018 New Series Banknotes

- The new \$100 notes are expected to be issued this year, and the \$20 and \$50 notes before 2020 Chinese New Year.

Coin Collection Programme

- Two Coin Carts collect coins from members of the public in 18 districts on a rotational basis.
- 568,000 people have been served and 466 million coins with a total face value of HK\$657 million have been collected since inception in October 2014.

Collaboration with Big Waster

- The HKMA collaborated with Big Waster (the mascot of the Environment Bureau) to jointly promote the use of good-as-new banknotes for lai-see in the Chinese New Year through social media videos.



GOVERNMENT BOND PROGRAMME

- To issue the fourth batch of Silver Bond in 2019 targeting Hong Kong residents aged 65 or above

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Institutional part – outstanding as at March 2019

- 13 Government bonds totalling HK\$76 billion
- Three Islamic bonds totalling US\$3 billion

Retail part – outstanding as at March 2019

- One iBond and three Silver Bonds totalling HK\$18.7 billion

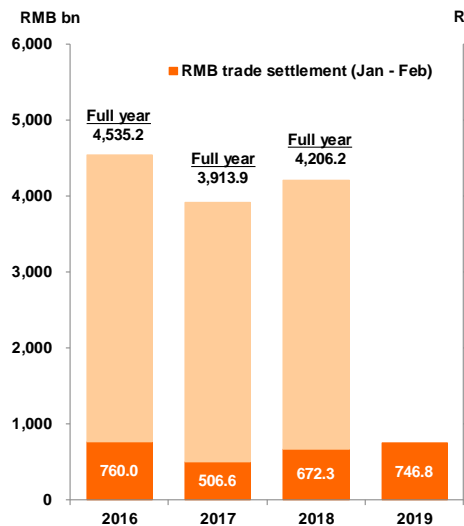


HONG KONG AS AN INTERNATIONAL FINANCIAL CENTRE

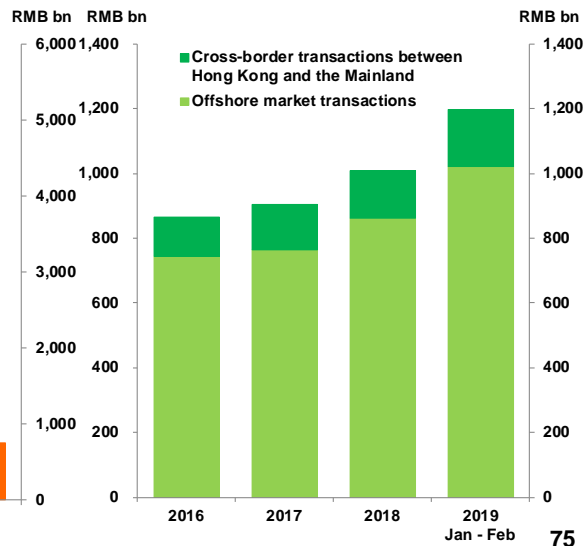


RMB TRADE SETTLEMENT AND PAYMENT

**RMB trade settlement
handled by banks in Hong Kong**



**Average daily turnover of Hong Kong
RMB RTGS System**

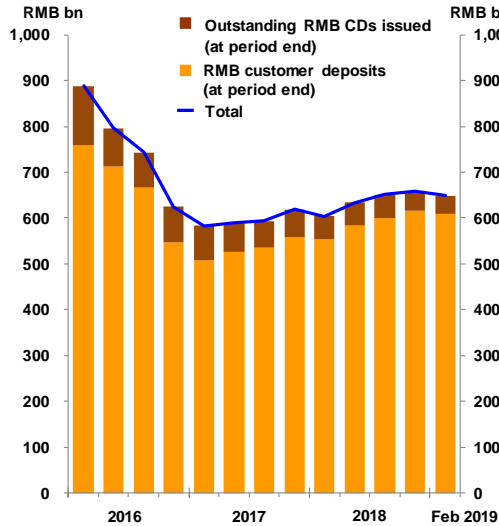


- In the first two months of 2019, renminbi trade settlement handled by banks in Hong Kong totalled RMB746.8 billion.
- In the first two months of 2019, the average daily turnover of Hong Kong RMB Real Time Gross Settlement (RTGS) system stood at RMB1,199 billion.

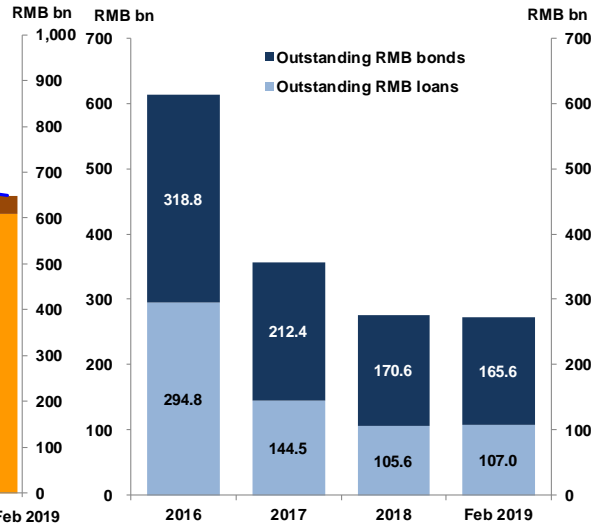


RMB LIQUIDITY POOL AND FINANCING ACTIVITIES

RMB customer deposits and certificates of deposit (CDs)



RMB financing activities



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- At end-February 2019, renminbi customer deposits and outstanding renminbi CDs amounted to RMB608.3 billion and RMB40.3 billion respectively, totalling RMB648.6 billion.
- At end-February 2019, outstanding renminbi loans amounted to RMB107.0 billion. Outstanding dim sum bonds amounted to RMB165.6 billion. The dim sum bond issuance totalled RMB1.4 billion for the first two months of 2019.



MAINTAINING RMB BUSINESS LINKS WITH OTHER JURISDICTIONS

	Feb 2019	2018	2017	2016
1 No. of participating banks of Hong Kong's RMB clearing platform	200	200	203	210
Of which:				
Branches and subsidiaries of overseas banks and overseas presence of Mainland banks	173	173	178	184
2 Amount due to overseas banks (RMB billion)	87.3	80.4	95.4	69.0
3 Amount due from overseas banks (RMB billion)	152.4	132.8	131.3	91.6

- The HKMA continued to expand and deepen its ongoing collaboration with other overseas economies, including Australia, the UK, France and Switzerland, in offshore renminbi business and other areas of financial services. We also continued our marketing efforts through participation in industry events to promote Hong Kong's unique role as the gateway to Mainland China.



PROMOTING GREEN FINANCE

- Hosted the launch of Climate Bond Initiative's (CBI) Hong Kong Green Bond Market Briefing Report in February 2019
 - This is the first time that the CBI publishes a report on the Hong Kong green bond market and the report shows that Hong Kong market has been growing robustly. In 2018, green bonds arranged and issued in Hong Kong totalled US\$11 billion, more than three times the amount in 2017
- Taking forward the preparatory work for implementation of the Government Green Bond Programme
- Planning more measures to further promote Hong Kong's green finance platform



DEVELOPING A LIMITED PARTNERSHIP PLATFORM FOR PRIVATE EQUITY (PE) FUNDS

- At present, PE fund activities in Hong Kong are robust. The total capital under management by PE funds in Hong Kong reached US\$159 billion at end-2018
- PE funds active in Hong Kong generally exist in the form of offshore limited partnerships (LPs) because of tax reasons and Hong Kong's lack of a limited partnership vehicle suitable for PE fund operations
- An interdepartmental Taskforce chaired by Financial Services Branch and comprising Treasury Branch, HKMA, Inland Revenue Department and Securities and Futures Commission had made amendments to the relevant tax provisions to provide for tax exemption for onshore and offshore PE funds. The new regime has taken effect on 1 April 2019
- The Taskforce is now developing legislative proposal for a new LP for PE funds and a more competitive tax arrangement to attract PE funds to set up and operate in Hong Kong



INVESTMENT ENVIRONMENT AND PERFORMANCE OF THE EXCHANGE FUND

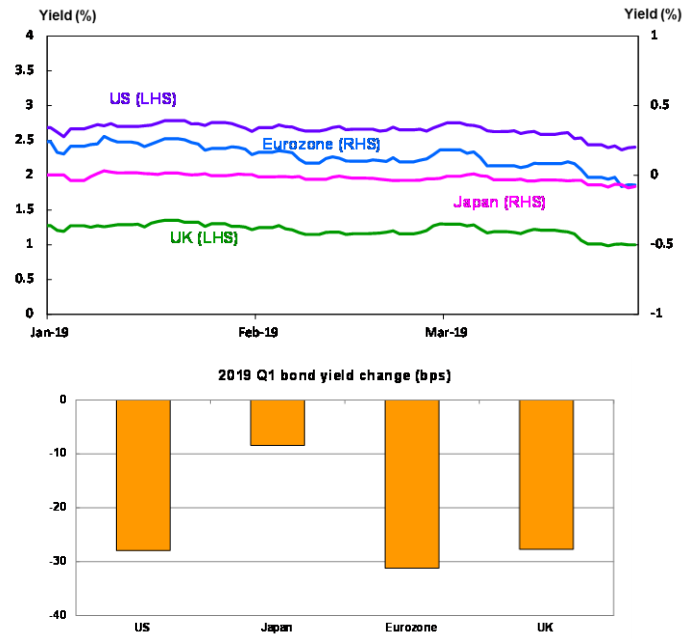


INVESTMENT ENVIRONMENT IN Q1 2019

- **Interest rates:** 10-year US Treasury yield initially traded in a tight range between 2.6% and 2.8% until March when it fell significantly to around 2.4% at month-end amid changing monetary policy stance of the US Federal Reserve. In particular, a “yield curve inversion” took place (i.e. long-term yields fell below short-term yields) in late March
- **Equity markets:** After significant corrections in Q4 last year, global equity markets rebounded significantly this quarter given progress in US-China trade talks and more dovish monetary policy stance taken by major central banks
- **Exchange rates:** Major currencies performed differently against the US dollar in the quarter: Renminbi and pound sterling strengthened against the US dollar, while euro weakened



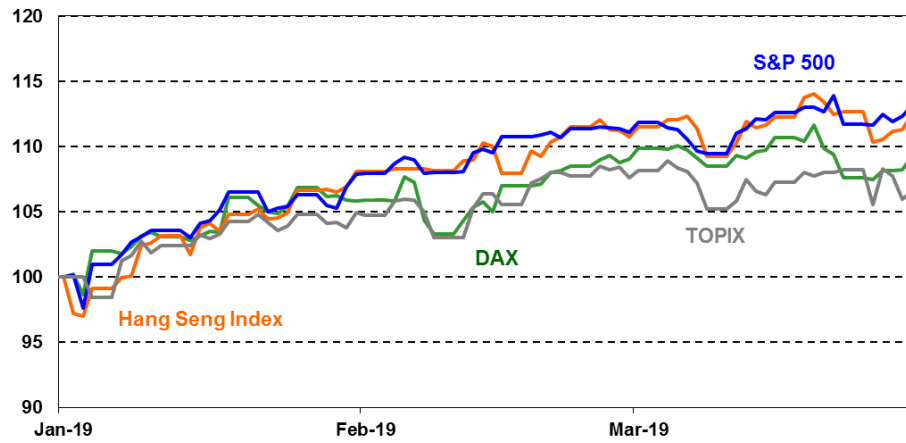
CHANGES IN 10-YEAR GOVERNMENT BOND YIELDS IN Q1 2019





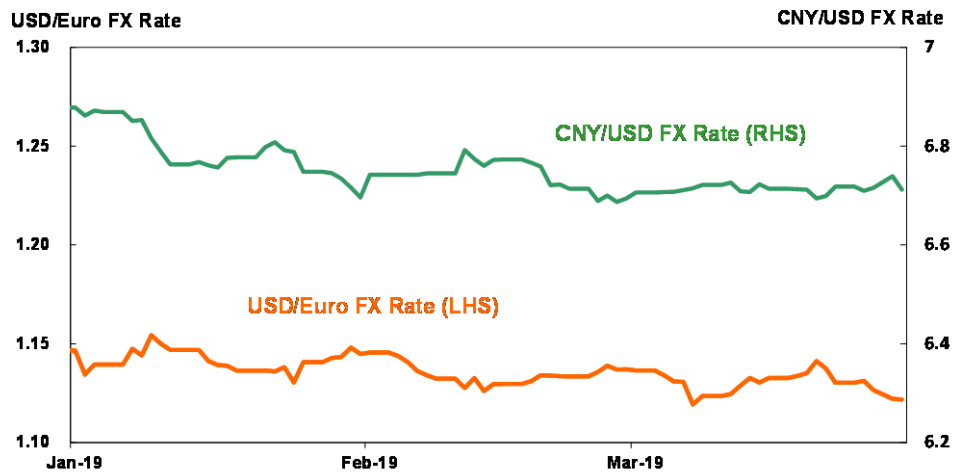
EQUITY MARKETS IN Q1 2019

Normalised Index Level (2018 year-end = 100)





CURRENCY MARKETS IN Q1 2019





INVESTMENT INCOME

	2019	2018	2017
	(unaudited)		
(HK\$ billion)	Q1	Full Year	Full Year
Bonds	36.7	57.4	34.4
Hong Kong equities*	20.8	(20.7)	58.3
Other equities	49.9	(38.7)	80.4
Foreign exchange[#]	13.5	(9.0)	53.5
Other investments[@]	-	21.9	37.4
Investment income	120.9	10.9	264.0

* Excluding valuation changes of the Strategic Portfolio.

[#] This is primarily the effect of translating foreign currency assets into Hong Kong dollar after deducting the portion for currency hedging.

[@] Including valuation changes of private equity and real estate investments held under the Long-Term Growth Portfolio. Valuations of these investments for the first quarter of 2019 are not yet available.



INCOME AND EXPENDITURE

	2019	2018	2017
	(unaudited)		
(HK\$ billion)	Q1	Full Year	Full Year
Investment income	120.9	10.9	264.0
Other income	-	0.2	0.2
Interest and other expenses	<u>(5.3)</u>	<u>(17.9)</u>	<u>(9.9)</u>
Net income/(loss)	115.6	(6.8)	254.3
Fee payment to Fiscal Reserves*#	(7.7)	(60.2)	(46.2)
Fee payment to HKSAR government funds and statutory bodies*	(2.2)	(13.8)	(8.6)

* The rate of fee payment is 2.9% for 2019, 4.6% for 2018 and 2.8% for 2017.

This does not include the 2019 fee payment to the Future Fund because such amount will only be disclosed when the composite rate for 2019 is available.

(The composite rate was 6.1% for 2018 and 9.6% for 2017. Fee payable to the Future Fund was HK\$16.4 billion for 2018 and HK\$22.7 billion for 2017.)



EXCHANGE FUND ABRIDGED BALANCE SHEET

(HK\$ billion)

ASSETS

	At 31 Mar 2019 (Unaudited)	At 31 Dec 2018	At 31 Dec 2017
Deposits	326.2	325.7	346.9
Debt securities	2,894.4	2,825.2	2,761.6
Hong Kong equities*	199.8	175.5	204.2
Other equities	507.7	452.3	507.5
Other assets [#]	<u>243.1</u>	<u>276.2</u>	<u>195.1</u>
Total assets	<u>4,171.2</u>	<u>4,054.9</u>	<u>4,015.3</u>

LIABILITIES AND EQUITY

Certificates of Indebtedness	500.7	485.7	456.7
Government-issued currency notes & coins in circulation	12.9	12.6	12.2
Balance of the banking system	64.8	78.6	179.8
Exchange Fund Bills and Notes issued	1,062.7	1,129.6	1,045.8
Placements by banks and other financial institutions	56.3	56.3	59.4
Placements by Fiscal Reserves [®]	1,188.1	1,173.5	1,073.8
Placements by HKSAR government funds and statutory bodies	313.2	320.6	305.1
Placements by subsidiaries	8.1	7.7	-
Other liabilities	<u>248.6</u>	<u>180.0</u>	<u>169.4</u>
Total liabilities	<u>3,455.4</u>	<u>3,444.6</u>	<u>3,302.2</u>
Accumulated Surplus	715.2	609.7	713.1
Revaluation Reserve	<u>0.6</u>	<u>0.6</u>	<u>-</u>
Total equity	<u>715.8</u>	<u>610.3</u>	<u>713.1</u>
Total liabilities and equity	<u>4,171.2</u>	<u>4,054.9</u>	<u>4,015.3</u>

* Including shares of the Hong Kong Exchanges and Clearing Limited in the Strategic Portfolio.

[#] Including fund injection to Exchange Fund's investment holding subsidiaries at a carrying amount of HK\$164.0 billion at 31 Mar 2019 (HK\$162.4 billion at 31 Dec 2018 and HK\$135.2 billion at 31 Dec 2017).

[®] Including placements by the Future Fund of HK\$224.5 billion.



HISTORICAL INVESTMENT INCOME

(HK\$ billion)

Year	Full Year	Q4	Q3	Q2	Q1
2001	7.4	13.6	10.4	(2.0)	(14.6)
2002	47.0	26.3	(2.1)	26.5	(3.7)
2003	89.7	33.5	8.4	41.1	6.7
2004	56.7	33.0	14.1	(7.2)	16.8
2005	37.8	7.3	19.0	13.6	(2.1)
2006	103.8	36.0	37.1	12.5	18.2
2007*	142.2	33.4	61.8	26.3	20.7
2008*	(75.0)	8.3	(48.3)	(20.4)	(14.6)
2009*#	107.7	10.6	71.9	58.7	(33.5)
2010*#	79.4	5.9	74.5	(12.1)	11.1
2011*#	27.1	22.1	(41.4)	21.6	24.8
2012*#	111.6	30.3	42.4	(5.6)	44.5
2013*#	81.2	30.7	54.7	(23.3)	19.1
2014*#	44.7	6.1	(17.8)	43.3	13.1
2015*#	(15.8)	21.0	(63.8)	18.7	8.3
2016*#	68.1	(23.3)	47.1	18.9	25.4
2017*#	264.0	66.0	61.8	71.3	64.9
2018*#	10.9	(33.6)	9.5	0.0	35.0
2019* (unaudited)	N/A	N/A	N/A	N/A	120.9

* Excluding valuation changes of the Strategic Portfolio.

Including valuation changes of private equity and real estate investments held under the LTGP.



HONG KONG MORTGAGE CORPORATION



MORTGAGE INSURANCE PROGRAMME (MIP)

- Since its launch in March 1999, the MIP has helped over 143,000 families attain home ownership
- In the first three months of 2019, the total number of loans drawdown and aggregate loan amount under the MIP were 1,625 cases and HK\$6.3 billion respectively, as compared to 2,451 cases and HK\$9.2 billion in the corresponding period last year
- About 69% of drawn down loans were for secondary market properties



REVERSE MORTGAGE PROGRAMME

- As at end-Mar 2019, 3,221 applications had been received:
 - Average age of borrowers: 69 years old
 - Average monthly payout: HK\$15,400
 - Payment terms: 10-year (25.6%), 15-year (15.5%), 20-year (12.6%), life (46.3%)
 - Average property value: HK\$5.3 million
 - Average property age: 30 years

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- Note: Figures in percentage for individual items may not add up to 100% due to rounding.



SME FINANCING GUARANTEE SCHEME (SFGS)

- Extension of application period of the 80% guarantee product and continuation of the following enhancement measures until end of June 2020: (1) reducing guarantee fee rates by 50%; (2) increasing maximum loan amount from \$12 million to \$15 million; and (3) lengthening maximum loan guarantee period from 5 years to 7 years
- As at end-March 2019, 15,148 applications had been approved, involving a total loan amount of around HK\$61.6 billion.

Average guarantee period	4.6 years	Enterprises with less than 50 employees	91%
Average loan size	HK\$4.07 million	Benefitted enterprises and the related no. of employees	8,609 enterprises and 221,342 employees
Average loan interest rate and average guarantee fee rate	4.93% p.a. 0.48% p.a.		

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- Industry types of approved applications for 80% loan guarantee product:

Manufacturing sector	20.8%
– Textiles and clothing	3.8%
– Electronics	1.9%
– Plastics	1.7%
– Printing and publishing	1.5%

Non-manufacturing sector	79.2%
– Trading	45.4%
– Wholesale and retail	9.6%
– Engineering	3.5%
– Construction	3.3%



LIFE ANNUITY SCHEME

- The three enhancement measures and the continuous sales model launched in mid-December 2018 have received positive response from the public. The operation has so far been smooth and provided good customer experience in terms of clarity and flexibility.
- Key statistics are as follows:

	1st Tranche of Sale (26 Sep – 12 Dec 2018)	Continuous Sales Model (13 Dec 2018 – 31 Mar 2019)
Total premium amount	HK\$2,689,160,000	HK\$503,350,000
No. of policies issued	5,305	632
Average premium amount	HK\$506,910	HK\$796,440